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KOREA
STAFF APPRAISAL REPORT
ON THE
CITIZENS NATIONAL BANK (CNB)

March 7, 1980

East Asia and Pacific Projects Department
Industrial Development and Finance Division

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CURRENCY EQUIVALENTS

US\$1.00	=	Won 580 /1
W 1	=	US\$0.0017
W 1 million	=	US\$1,724
W 1 billion	=	US\$1.72 million

ABBREVIATIONS

ADB	-	Asian Development Bank
BOK	-	Bank of Korea
CNB	-	Citizens National Bank
EPB	-	Economic Planning Board
FFYP	-	Fourth Five-Year Plan
IRF	-	Industrial Rationalization Fund
KCGF	-	Korea Credit Guarantee Fund
KDB	-	Korea Development Bank
KDFC	-	Korea Development Finance Corporation
KFX	-	Korea Foreign Exchange
KFSB	-	Korea Federation of Small Business
MCI	-	Ministry of Commerce and Industry
MOF	-	Ministry of Finance
NACF	-	National Agricultural Cooperative Federation
NFC	-	National Fisheries Cooperative
NIF	-	National Investment Fund
SMI	-	Small and Medium Industries
SMIB	-	Small and Medium Industry Bank
SMIPC	-	Small and Medium Industry Promotion Corporation
SMIPF	-	Small and Medium Industry Promotion Fund
SSI	-	Small-Scale Industries

FISCAL YEAR

January 1 - December 31

/1 Before January 12, 1980, the rate was W 485 to US\$1.00.

KOREA

THE CITIZENS NATIONAL BANK

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KOREA

THE CITIZENS NATIONAL BANK

Basic Data

(As of September 30, 1979, unless otherwise stated)

1. Year of Establishment: 1962

2. <u>Ownership:</u>	<u>Paid-in share capital /a</u>	
	<u>Won million</u>	<u>Percent</u>
Government of Korea	3,279.4	65.6
Commercial banks	1,706.3	34.1
Others	14.3	0.3
<u>Total</u>	<u>5,000.0</u>	<u>100.0</u>

3. Operations (Won million):

	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>Jan.-Sept. 1979</u>
<u>Approvals /b</u>				
Working capital loans	108,996	169,163	152,463	136,539
Equipment loans	11,822	17,332	17,093	15,442
<u>Total Business Loans</u>	<u>120,818</u>	<u>186,495</u>	<u>169,556</u>	<u>151,981</u>
General populace loans /c	87,984	108,488	170,984	152,308
<u>Total Approvals</u>	<u>208,802</u>	<u>294,983</u>	<u>340,540</u>	<u>304,289</u>
<u>Outstanding</u>				
Working capital loans	143,548	174,634	205,429	257,745
Equipment loans	21,642	28,738	32,285	36,040
<u>Total Business Loans</u>	<u>165,190</u>	<u>203,372</u>	<u>237,714</u>	<u>293,785</u>
General populace loans /c	87,884	130,468	196,261	229,204
<u>Total Outstanding</u>	<u>253,074</u>	<u>333,840</u>	<u>433,975</u>	<u>522,989</u>

4. Earnings Record (percentages):

Net income as % of average equity	11.4	11.5	20.6
Financial expenses as % of average total assets	7.6	8.9	8.6
Administrative expenses as % of average total assets	3.8	3.6	3.7
Book value as % of par	183	187	222
Dividend payout ratio	35	37	19

/a Paid-in share capital is being increased by W 25 billion (W 11.2 billion in cash and W 13.8 billion in assets revaluation) with equal participation by the Government and commercial banks.

/b Given the nature of domestic currency operations, approvals are simultaneous with commitments and disbursements.

/c Including households and individuals.

5. Financial Position (Won million):

	1976	1977	1978	Sept. 30 1979
Total assets	371,573	591,024	868,792	1,113,396
Of which total loan portfolio	253,074	333,840	433,975	522,989
Of which term loan portfolio	244,824	323,325	406,269	443,571
Long-term debt	160,661	245,641	345,817	393,663
Equity	8,234	9,370	11,076	26,911
Current ratio	1.07	1.05	1.19	1.09
Total debt/equity ratio	44.1	62.1	77.4	40.4
Long-term debt/equity ratio <u>/a</u>	14.5	21.7	24.2	9.3
Reserves and provisions as % of loan portfolio	1.87	1.61	1.60	4.52

6. CNB's Interest Rates and Charges (effective from
January 12, 1980): /b

	% p.a.
<u>Foreign Currency Loans</u>	
ADB first loan	9.5
Korea foreign exchange fund	LIBOR + 1.5%
<u>Domestic Currency Loans</u>	
<u>Equipment Loans</u>	
Mutual installment savings	21.16 - 24.08
Bills	24.5 - 25.0
<u>Working Capital Loans</u>	
Remuneration basis	21.16 - 24.08
Bills, discount on bills, installment savings	} 24.5 - 25.0
Overdrafts	26.5 - 27.0
<u>General Populace Loans</u>	
Remuneration basis	21.16 - 24.08
With savings as collateral	25.0
Bills, installment savings	25.0
Penalty charges on overdue loans	40.0

/a After excluding current maturities.

/b In line with the practice of Korean government-owned financial institutions in relending foreign exchange resources borrowed from official sources (IBRD, ADB, et al), CNB charges a uniform spread of two percentage points above its borrowing rate.

1. THE INDUSTRIAL SECTOR

Contribution to the Economy

1.01 Since the early 1960s, the industrial sector, and more specifically manufacturing,^{/1} has been the engine of growth of the Korean economy. Over the period 1974-78, the manufacturing sector has grown at an average 17% p.a. in real terms compared to an average 10.3% growth of aggregate GNP. As a consequence of this faster growth rate, the share of manufacturing in total GNP has increased from about 20% in 1971 to nearly 32% in 1978. By end 1978, manufacturing employment reached just over 3 million and accounted for 22.4% of the total employed population compared to 15.9% in 1973. Over the five year period 1974-78, approximately 1.2 million jobs have been created in the manufacturing sector; this represented 58% of total employment creation during that period.

1.02 Export Orientation and Export Dependence. Korea's success story in economic development is largely based on a strategy of export promotion with particular emphasis on manufactured exports. Total commodity exports just exceeded US\$10 billion in current prices in 1977 and reached US\$12.7 billion in 1978. Manufactured goods, which accounted for about 52% of total exports in 1964, have gradually increased their share and have remained at about 90% for the past three years. It is estimated that export expansion contributed about 35% of manufacturing output growth over the period 1975-77 against 74% for domestic demand.^{/2} Gradual changes have taken place in the structure of manufactured exports over the past three years: light manufactured products including textiles have declined in relative terms from 56% to 53%; machinery, transport equipment and chemicals have increased their share from 18% in 1974 to 22% in 1977; some of Korea's traditional light exports such as footwear and clothing have remained buoyant, edging up from 26.7% to 28.4%.

1.03 The growth rate of commodity exports slowed down in real terms to about 15.8% p.a. over the period 1977-78 compared to an average of 32.7% over the period 1972-76. The 15.8% p.a. growth rate of real exports was in fact lower than 17% average annual growth in manufacturing, which seems to indicate the growing importance of the domestic market for the manufacturing sector. This may prove a favorable development considering that until 1977 the export dependence of the manufacturing sector had been rising faster than expected. The ratio of manufactured exports to output reached 28.3% in 1977

^{/1} In 1978, manufacturing alone accounted for 96% of total value added (in 1975 prices) in the industrial sector (i.e. mining and manufacturing).

^{/2} Import substitution made a negative (-9%) contribution.

with considerable variations in the dependence ratio between the various subsectors./1 The ratio of commodity exports to GNP had likewise increased from 26.7% in 1975 to 34.4% in 1978.

Structural Changes in Manufacturing

1.04 The growth of the manufacturing sector has been accompanied by significant adjustments in the structure of production by the various component subsectors as shown in the following table:

Table 1: COMPOSITION OF VALUE ADDED IN MANUFACTURING, 1970-78
(W billion in 1975 prices)

	<u>1970</u>		<u>1974</u>		<u>1978</u>	
	Amount	%	Amount	%	Amount	%
<u>Light Industries</u>						
Textile	176.9	15.6	425.0	18.5	710.1	16.3
Others	484.0	42.6	798.9	34.7	1,336.3	30.7
Subtotal	<u>660.9</u>	<u>58.2</u>	<u>1,223.9</u>	<u>53.2</u>	<u>2,046.4</u>	<u>47.0</u>
<u>Heavy Industries</u>						
Basic metals	26.9	2.4	102.1	4.4	224.9	5.2
Machinery /a	111.1	9.8	361.0	15.7	971.2	22.3
Chemicals /b	336.7	29.6	614.1	26.7	1,107.4	22.5
Subtotal	<u>474.7</u>	<u>41.8</u>	<u>1,077.2</u>	<u>46.8</u>	<u>2,303.5</u>	<u>53.0</u>
<u>Total Manufacturing</u>	<u>1,135.6</u>	<u>100.0</u>	<u>2,301.1</u>	<u>100.0</u>	<u>4,349.9</u>	<u>100.0</u>

/a Including fabricated metal products.

/b Including paper and paper products, petroleum and nonmetallic mineral products.

Source: Table 8.13. World Bank Economic Report dated May 15, 1979.

1.05 The composition of manufacturing shows a marked shift in favor of the heavy and chemical sectors which exceeded 50% of total manufacturing value added for the first time in 1978. The most significant gains have

/1 The export output ratio reached a level of 67% for wood and furniture and 91% for miscellaneous products in 1977.

been registered by the machinery sector. The rate of growth of chemical industries, however, lagged behind the aggregate manufacturing sector and their share consequently declined from about 30% in 1970 to 22.5% in 1978. Light industries have declined steadily since 1970. The sharpest declines were recorded in the food, beverage and tobacco sector. Textiles have been maintaining their 16-17% share of total manufacturing value added. In fact, textile yarn and fabric industries have lost ground but this was compensated by the good performance of footwear and clothing. The changes in the structure of manufacturing reflect a deliberate policy gradually to shift production from Korea's traditional light industrial production towards more skill- and technology-intensive types of production.

Geographic Distribution

1.06 The 1975 population census showed that approximately 27% of the population of Korea lived in the cities of Seoul and Busan; the province of North Gyeongsang in which Taegu, the third largest industrial city is located accounted for another 14%. The following table shows that the regional distribution of manufacturing enterprises and employment is even more skewed in favor of Seoul and Busan.

Table : GEOGRAPHIC DISTRIBUTION OF INDUSTRY
(%)

	1974			1977		
	No. of enterprises	No. of workers	Value added	No. of enterprises	No. of workers	Value added
Seoul and Pusan	34.6	48.7	44.5	38.6	46.2	37.5
Other regions	665.4	51.3	55.5	61.4	53.8	60.5
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: Report on Mining and Manufacturing Survey. EPB 1977.

While Seoul and Pusan remain the largest industrial centers, marginal improvements have taken place between 1974 and 1977 in the redistribution of industrial employment outside of these areas. This may be the first sign that Government policies aimed at a better distribution of employment are paying off. Government policies aiming at a reduction of the congestion of Seoul and Pusan include severe restrictions on industrial expansion in these two cities, a program of financial assistance for the relocation of industries, the promotion of new industrial estates such as the Pohang, Ulsan and Yeosu complexes and the Saemaeul Movement initiated in 1971 for creating off-farm employment in rural areas.

Factor Use and Efficiency

1.07 The main elements which have contributed to the expansion of the manufacturing sector are the rate of investment and efficiency in factor use, both capital and labor.

1.08 Gross Fixed Capital Formation. Over the period 1969-75, manufacturing generally accounted for less than 20% of aggregate fixed capital formation. Over the period 1975-77, it reached an average of 21.9%. In 1978, total fixed investment increased by a phenomenal 40.5% in real terms; the manufacturing sector outpaced this growth and reached 58.3% in real terms thus increasing its share of total fixed investment to 23.8%. Within the manufacturing sector the share of the heavy and chemical sector in total gross domestic capital formation increased significantly from 46% in 1973 to 52.9% in 1976 and 56.2% in 1978. The recent growth rates of GDCF substantially exceed those projected in the FFYP; the revised plan for 1979-81 projects a slowdown in the growth of GDCF from 30.1% for the period 1977/78 to 12.9% p.a. Although no sectoral breakdown of investment is available, the manufacturing sector is expected to increase further its share and manufacturing investment should therefore grow at a slightly higher rate than aggregate investment.

1.09 Factor Efficiency. Efficiency of the manufacturing sector in its utilization of capital investment can be measured by the incremental capital to output ratio (ICOR). Calculations of ICORs with a one-year lag show a gradual decline over the three consecutive periods 1961-66, 1966-71 and 1971-75, thus indicating increasing efficiency in the use of capital investment. Inclusion of data for 1976 and 1977 raises the ICOR estimate to 1.012/¹ for the period 1971-77 compared to 0.977 /¹ for the period 1971-75. This may reflect the higher capital intensity of investment in manufacturing in recent years because of the larger share of the heavy and chemical sectors. Efficiency in capital utilization is also evidenced by the growth in industrial capacity utilization which reached an average of 7.2% over the period 1963-71 and 3.4% p.a. over 1971-77. Capacity utilization had reached by 1971 a level comparable to that of developed countries. Labor productivity as measured by the ratio of value added per employee has been increasing in all manufacturing subsectors over the period 1970-76 and was sufficient to absorb wage increases. Over the period 1977-78, however, productivity gains have lagged behind the rapid growth in real wages.

Financial Structure of Enterprises

1.10 Surveys of the capital structure of manufacturing enterprises indicate a high reliance on debt financing. The average aggregate debt/equity ratio of manufacturing enterprises which stood at 2.7:1 in 1973 following the financial measures of 1972 increased to 3.2:1 in 1974 and

¹ Based on 1970 constant prices.

averaged 3.6:1 over the period 1976-78. The long-term debt/equity ratio, however, reached only 1.5:1 in 1978, reflecting the larger share (58%) of short-term borrowings in total borrowings. The average interest rate paid on borrowings, short- and long-term, ranged from 12% to 13% over the period 1976-78. Profitability measured in terms of net income to total assets has declined marginally from 3.2% in 1976 to 2.7% in 1978 but remained quite satisfactory.

Industrial Policies

1.11 The phenomenal growth of the manufacturing sector was to a large extent made possible by efficient and pragmatic government policies. Incentive packages have been developed and adjusted over time to fit evolving priorities for industrial development. With variable emphasis, policies have aimed at the promotion of export industries, import substitution, assistance to small and medium enterprises, geographic dispersal of industry and in the last few years, promotion of skill-intensive sectors with a higher technological content. Export promotion has been the major objective since the early sixties until the recent past. Concerns have surfaced recently about the desirability of maintaining the same degree of priority on export expansion because of a potentially dangerous situation of export dependence for the Korean economy and because of the inflationary impact of export promotion in the face of rising domestic demand. Subsidies on exports have continued to increase in absolute terms over the period 1975-78 but were insufficient to compensate for the loss of competitiveness induced by higher Korean prices relative to its major trading partners. As a result, the real effective exchange rate deteriorated sharply for Korean exporters over that period.

1.12 Export Incentive System. Government incentives to exporting industries include tax exemption, accelerated depreciation allowances, refund of import duties on raw materials used for export production, deferred payment of tariffs on equipment and access to subsidized credit. These incentives are administered within the framework of an export targeting system whereby exporting firms set for themselves certain export targets in agreement with overall government objectives. A monthly conference is held to review and adjust targets as well as government policies affecting their implementation.

1.13 While the emphasis has clearly been on export promotion, key import substitution industries have received substantial government support in the form of partial tax and tariff exemptions, as well as protection from competing imports. Production for the domestic market, however, has generally been subject to higher duties, taxes, and interest charges on borrowings. In 1977-78, the Government has relaxed a number of import restrictions as part of an import liberalization program to be implemented over a four-year period. Banned items have been abolished; since January 1, 1979, 69% of all import items are subject to automatic approval, 31% are

"restricted".^{/1} Tariff adjustments have also been introduced to improve the competitiveness of import substituting industries. The simple average tariff rate has been reduced from 36% to 25%.

Recent Performance

1.14 The performance of the Korean economy in the first two years (1977-78) of the Fourth Five Year Plan (FFYP) period has exceeded the ambitious plan targets. The average annual growth rate of GNP reached 11.5% in real terms compared to the 9.5% envisaged in the plan for 1977 and 1978. Due to unexpected gains in Korea's terms of trade, the real gross national income grew by almost 28%, nearly reaching in two years the growth targeted in the first three years of the FFYP. The per capita income in current US dollars reached \$1,242 in 1978. The growth rate of investment was twice as high as that of GNP in 1977 and three times as high in 1978. With the relative decline in the share of investments in inventories, the rate of increase in gross fixed capital formation was even faster than in total investment. Manufacturing, transport and dwellings accounted for 83% of the increase in gross fixed capital formation in 1978. In spite of this phenomenal growth in real investment during 1977-78, Korea's reliance on foreign savings has declined compared to the 1972-76 period as a result of a remarkable improvement in national savings. The national saving income ratio has increased from 18% in 1975 to 25.6% in 1977 and 27.2% in 1978.

1.15 The industrial sector has provided a major impetus to GNP growth over the period 1977-78. The growth rate of the manufacturing sector averaged 17% p.a. in real terms over that two-year period, considerably exceeding the FFYP target of 15.8% p.a. During the period 1977-78, the overall rate of growth of employment reached 3.7% p.a. but manufacturing employment grew at 6.1% p.a. Manufacturing accounted for 22.4% of total employment in 1978. Real wages in the manufacturing sector increased at an average of 19.5% during 1977-78, substantially in excess of productivity gains which reached 11.3% p.a. This may to some extent reflect a tightening of the labor market particularly the increasing demand for skilled labor.

Prospects

1.16 The stresses imposed on the Korean economy by the rapid pace of growth over the period 1977-78 have prompted the Government to initiate a stabilization program in April 1979. The FFYP has been revised accordingly and a new Economic Management Plan was introduced for the remaining plan period of 1979-81. The main elements of the Government's program include a deliberate slowdown in GNP growth, reduction in the growth rate of credit and money supply, a moderate pursuit of export growth and greater emphasis

^{/1} In early 1978, 54% of all items were subject to automatic approval, 41% were restricted and 5% were banned.

on light industries geared to the domestic market. GNP growth is expected to slow down from 11.5% to 9.3% during 1979-81. The growth of value added in the manufacturing sector would decline from 19.7% in 1978 to an average of 13.5% for 1979-81. Domestic investment would also be reduced from 30% to about 13% p.a. On January 12, 1980, Korea devalued the won by 16.55% from W 485 to W 580 to the US dollar in an attempt to promote the competitiveness of its exports. It is expected that such a measure will increase the momentum of increased production and exports, which showed signs of slowing down in the second half of 1979. The devaluation is one step towards achieving an expanded economy based on enlarged exports, which will remain the engine of economic growth.

2. THE SMALL INDUSTRY SECTOR

Definition

2.01 A support program aimed specifically at smaller enterprises was initiated by the Government in the early 1960s with the enactment of the Small and Medium Industry Cooperative Law, the Small and Medium Industries Basic Act and the special act establishing the Small and Medium Industry Bank (SMIB). These laws generally aimed at reducing overcompetition and at fostering the modernization and rationalization of production by smaller industries. No distinction is made in Korea between medium-sized and small enterprises; both are entitled to the same degree of support. The cutoff point between small and medium industries (SMI) and their larger competitors has been adjusted upwards over time to take account of the economic development of the country and of inflationary pressures. The present limitation which has been in effect since January 1977 is set in terms of employment or total assets as indicated below:

Sector	Total assets (W million)	<u>or</u>	No. of employees
<hr/>			
Mining, manufacturing and transportation	500		300 <u>/a</u>
Construction	500		50
Commerce and services	50		20

/a The 1979 Enforcement Decree of the Small and Medium Industry Promotion Law raises the employment criterion to 500 for selected industries including automobile parts, electronic products, cycle parts, etc.

In applying for financial assistance, enterprises which exceed both of the above criteria must apply to the Korea Development Bank (KDB) which only caters to large firms; enterprises which satisfy either of the above criteria (and have more than five employees) can approach SMIB.

2.02 The Citizens National Bank (CNB) was established in 1972 for the purpose of mobilizing household savings and for making available to its depositors small consumer and business loans. The scope of its operations has been gradually expanded to include payment guarantees, transactions in foreign currency and, since 1977, borrowing and lending in foreign currency. Over time, CNB has been placing increasing emphasis on lending for small business. Government regulations which limited its lending to enterprises employing less than 50 persons have been relaxed in February 1977 to include enterprises employing up to 100 persons. The smaller segment of SMI is therefore eligible for financial assistance from both SMIB and CNB. In this report the small-scale industry (SSI) sector is notionally defined as the segment of SMI comprising enterprises employing up to 100 persons.

2.03 A sample survey of the SMI sector conducted in 1978 by the Korea Federation of Small Business (KFSB) indicates a high correlation between size of employment and total assets. The survey indicates that 92% of the total number of enterprises employing up to 100 persons had assets of less than W 200 million /1 and 98% had assets of less than W 500 million. /1 Given the impact of inflation in the past two years, it can be assumed that approximately 95% of the population of enterprises employing less than 100 persons would have assets of less than W 500 million in 1980 prices. Small scale industries in Korea can therefore be defined as enterprises employing less than 100 persons or having assets of less than W 500 million. The KFSB survey also shows a correlation between an employment size of 50 persons and assets of W 250 million (in 1980 prices). Indications are that an employment size of 300 can be linked with a total asset size of W 1.5 to 2 billion which shows that the delineation in terms of assets between size and large industries currently in force (para. 2.01) might need to be revised upwards.

Role of SSI in the Korean Economy

2.04 Annex 1 summarizes recent trends in the contribution of small, medium and large enterprises to the manufacturing sector. /2 SSI enterprises numbered 23,300 in 1977 or 87% of all manufacturing enterprises. /3 In the

/1 In 1977 current prices.

/2 The following analysis defined enterprises with less than 100 workers as small enterprises with 100 to 299 workers as medium and enterprises with over 300 workers as large.

/3 CNB's potential business clientele is however larger since it includes nonmanufacturing sectors as well namely mining, construction, transportation and trade.

same year, SSI enterprises employed 480,000 persons or 25% of total manufacturing employment and accounted for 16% of value added.

SIZE DISTRIBUTION OF MANUFACTURING, 1977

Employment size	No. of estab- lishments		No. of employees		Value added		Fixed capital formation	
	('000)	(%)	('000)	(%)	(W bil.)	(%)	(W bil.)	(%)
Small (5-99)	23,299	87.0	480	25.0	886	15.8	145	10.9
Medium (100-299)	2,382	8.9	403	21.0	929	16.6	220	16.5
Large (over 300)	1,085	4.1	1,036	54.0	3,782	67.6	971	72.6
<u>Total</u>	<u>26,766</u>	<u>100.0</u>	<u>1,919</u>	<u>100.0</u>	<u>5,597</u>	<u>100.0</u>	<u>1,336</u>	<u>100.0</u>

Source: EPB, 1977 Survey of Mining and Manufacturing.

The share of SSI in total manufacturing investment reached 10.9% in 1977, a ratio which has remained practically unchanged for the past four years except in 1976 when it peaked at 13.5%. No separate statistics are available to show SSI contribution to Korean exports, the export orientation of the SMI sector (including SSI) however is quite impressive: while SMI accounted for 31% of total manufacturing output in 1977, their share of total commodity exports reached 36.2%. This strong performance reflects to a large extent SMI responsiveness to government incentives for export orientation. Particularly effective in this respect are the subcontracting and cooperative arrangements whereby SMI improve the marketability of their production. A CNB survey indicates that export sales accounted for 16% of total SSI sales in 1976 with no more than 22% being exported directly by the producer. About 60% of SSI sales were actually sold on order from other firms or through subcontracting arrangements.

2.05 The following table shows the growth trends in small, medium and large enterprises over the period 1963-77. In 1963, SSI was the most important sector in terms of employment and generated 42% of total manufacturing value added. Over the following decade, however, the emphasis lay on the development of large industry whose rapid growth overshadowed the SSI sector. In recent years however, SSI enterprises have received more support and SSI value added has been growing at an average of 40% p.a. over the past five years, about the same rate as for medium and large enterprises. Labor productivity measured by the ratio of value added per employee reached 51% of productivity in large enterprises in 1977 compared to 47% in 1973. Productivity gains in SSI have apparently more than kept pace with those registered by larger enterprises.

GROWTH RATES IN MANUFACTURING 1963-77
(% p.a.)

	Employment			Value Added		
	1963-68	1968-73	1973-77	1963-68	1968-73	1973-77
Small (5-99 workers)	7.7	0.2	9.5	26.3	22.8	39.6
Medium (100-299 workers)	((19.1	((14.6	18.4	((43.8	((39.4	40.9
Large (over 300 workers)	((13.8	((42.8
<u>Total</u>	13.2	9.1	13.5	37.4	35.6	41.9

Source: EPB, 1977 Survey of Mining and Manufacturing.

Industrial Structure of SSI Sector

2.06 The subsectoral distribution of value added and employment by size of enterprise in 1977 is summarized below. In 1977, the four subsectors of textiles, fabricated metals, food products and chemicals together accounted for 71.5% of value added and 74.3% of employment in the SSI sector. While the sectoral distribution is not substantially different for medium and larger enterprises, it is interesting to note that the dependence on these four subsectors increases with the size of enterprises to reach 80% in medium industries and 83% in large industries for both value added and employment. Labor productivity within the SSI sector is lowest in textiles and highest in chemicals and nonmetallic minerals.

STRUCTURE OF THE MANUFACTURING SECTOR, 1977
(%)

	Value added				Employment			
	Small <u>/a</u>	Medium <u>/b</u>	Large <u>/c</u>	Total	Small <u>/a</u>	Medium <u>/b</u>	Large <u>/c</u>	Total
Food, beverages, tobacco	15.9	20.1	19.6	19.1	12.3	7.2	7.9	8.8
Textiles, clothing, leather	20.2	23.4	18.5	19.6	28.8	41.6	34.0	34.3
Wood and wood products	4.9	1.5	2.1	2.5	5.2	1.7	3.7	3.7
Paper and paper products	7.1	4.8	3.3	4.2	7.6	4.4	2.9	4.4
Chemicals, rubber, plastics	15.1	17.3	19.4	18.3	10.3	9.3	14.6	12.4
Nonmetallic minerals	9.7	7.6	3.6	5.2	5.0	5.2	3.1	4.0
Basic metals	3.9	3.4	6.9	5.8	3.4	3.3	4.0	3.7
Machinery and equipment	20.3	18.8	25.2	23.4	22.9	21.8	26.2	24.5
Other	2.9	3.1	1.4	1.9	4.5	5.5	3.6	4.2
<u>Total</u>								
<u>Manufacturing</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

- /a Enterprises employing 5-99 workers.
/b Enterprises employing 100-299 workers.
/c Enterprises employing over 300 workers.

Source: EPB. Report on Mining and Manufacturing, 1977.

Regional Distribution of SSI

2.07 The following table shows that in 1977 SSI employment was less concentrated in the main industrial areas of Seoul, Pusan and Gyonggi than either medium or large industries. SSI employment outside these areas reached 40% in 1977, compared with 31% only for medium and large enterprises.

REGIONAL DISTRIBUTION OF MANUFACTURING, 1977
(%)

	Value added			Employment		
	Small	Medium	Large	Small	Medium	Large
Seoul	30.8	26.0	23.3	30.3	30.1	26.1
Busan	13.3	13.6	12.1	12.4	15.3	22.0
Gyeonggi province	19.3	26.9	22.3	17.2	23.4	20.6
Other regions	36.6	33.5	42.2	40.1	31.2	31.3
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: EPB. Report on Mining and Manufacturing Survey, 1977.

It is interesting to note however that the share of large industry employment in Seoul and Pusan has been declining rapidly from 56% in 1972 to 50.5% in 1976 and 46.7% in 1977. This trend is the consequence of Government restrictions on the establishment of new large industries in these two cities and of a concerted policy of relocation of existing plants. Paradoxically, small and medium industries which are not subject to the same restrictions show an increased concentration in the Seoul area.

Fixed Capital Formation in SSI

2.08 Additions to fixed assets in the SSI sector can be estimated on the basis of the manufacturing surveys conducted annually by EPB. According to these surveys, fixed asset investment in the manufacturing sector increased in current terms from W 589 billion in 1974 to W 1,336 billion in 1977 which represents an average annual growth rate of 31.5%. Over the same period, SSI fixed assets investment fluctuated in relative terms but reached W 145 billion or 10.9% of total manufacturing investment in 1977 compared to W 65 billion or 11% in 1974. Over the four-year period 1974-77, SSI investment has kept pace with overall fixed capital formation in manufacturing. No drastic change is expected in the coming years. National income statistics show an upsurge in manufacturing investment of 67.5% in current terms

in 1978; on that basis SSI fixed investment would have reached W 243 billion in 1978. Based on the revised objectives of the Economic Management Plan for the period 1979-81, manufacturing investment can be expected to grow at a minimum average of 15% p.a. in current terms. SSI investment should keep pace with this rate of growth and reach W 280 billion in 1979, W 320 billion in 1980 and W 370 billion in 1981.

2.09 The BOK 1978 analysis of the financial structure of manufacturing enterprises suggests that investment in land and buildings accounts for about 40% of SMI fixed assets with the remaining 60% allocated to machinery and equipment. Another survey of SSI investment by CNB shows that similar ratios prevail in the small industry sector and indicates that foreign currency expenditures account for about 25% of total SSI investment in machinery and equipment. The foreign exchange demand of SSI sector for the period 1979-81 can therefore be estimated as follows:

	1978	1979	1980	1981
<hr/>				
Total SSI fixed investment (W billion)	243	280	320	370
Total SSI investment in machinery and equipment (W billion)	146	168	192	222
Foreign exchange demand (US\$ million)	75.3	86.6	99.0	114.4

2.10 Until 1978, SMIB was the only source of foreign exchange finance for SSI investment. Over the period 1976-78, the SSI sector /1 accounted for approximately 40% of SMIB's foreign exchange lending, reaching a high of US\$42 million in 1978. SMIB's foreign exchange lending is expected to expand at a rate of 7% p.a. over the coming years thus reaching US\$45 million in 1979, US\$48 million in 1980 and US\$51 million in 1981. SMIB's supply of foreign exchange would therefore cover less than half of estimated SSI demand. The gap between supply and demand would reach US\$41.6 million in 1979, US\$51 million in 1980 and US\$63.4 million in 1981. CNB having started its foreign currency lending operations in 1979 is expected to cover a part of this gap.

Financial Structure of SSI

2.11 An analysis of the financial structure and performance of SSI enterprises is available from SMIB's annual surveys of the SMI sector. The ratio of fixed assets to total assets was surprisingly high in 1977 for very small SMI enterprises but declined rapidly with size (74% for enterprises having 5 to 9 workers, 54% for 10-19 and 46% for 20-49). BOK statistics for

/1 i.e. enterprises employing less than 100 workers.

1978 show an average fixed assets ratio of 36% for the SMI sector /1 well below the 50% recorded by large enterprises./2 Assuming that the fixed assets ratio can be considered as a reliable indicator of production capacity and of capital utilization in the manufacturing sector, it appears that medium sized enterprises employing 100 to 300 workers are more efficient than both smaller and larger units. The total debt/equity ratio of SSI enterprises is very low reaching only 0.3:1 for enterprises with less than 9 workers and rising gradually to 1.8:1 for enterprises with 50-100 workers. These figures reflect the high reliance of SSI on self-financing; in 1977, the ratio of net worth to total assets reached 77% for 5-9 workers and declined to 36% for 50-100 workers. The unorganized money market (UMM) however accounted for a minor share of 6-14% (increasing in smaller enterprises) of total borrowings. Data on the source of funds of SSI investment confirm that in 1977 self-financing accounted for 60% of SSI fixed asset investments and the UMM for about 1.3%. In 1978, however, resources available to smaller SSI enterprises from financial institutions declined in relative terms and UMM borrowings financed about 8% of investment by enterprises with 5-20 workers. The profitability of SSI enterprises is markedly higher than for larger enterprises. Return on total assets reached 12% for the 5-9 worker category in 1977 and declined to 7.6% for 10-19 workers, 6.8% for 20-49 workers and 5.1% for 50-100 workers. By comparison, the same ratio stood at 2.6% for large enterprises.

Government Support for SSI

2.12 As indicated above, there is no Government assistance program aimed specifically at the smaller end of the SMI sector. Since the early 1960s, however, the Government has launched a number of programs and established institutions which support the "nonlarge" sector of industries labelled small and medium for the sake of convenience. CNB is the only institution which is limited to providing financial assistance to smaller enterprises with less than 50 workers until 1977 and less than 100 since then. The following paragraphs accordingly review the programs of government support for the SMI sector as a whole.

Nonfinancial Support of SMI

2.13 The Small and Medium Industry Basic Law, enacted in 1966, provides the main orientations of government support in favor of SMI enterprises. The primary objectives for the sector are (a) improvements in the production process and quality of SMI; (b) protection of SMI from unfair competition by larger industries; (c) establishment of linkages with larger industries; and

/1 i.e. enterprises employing 5 to 299 workers.

/2 employing over 300 workers.

(d) promotion of cooperative efforts. The Law also provides that appropriate amounts of financial assistance should be supplied to support these objectives. The Bureau of Small and Medium Industry of the Ministry of Commerce and Industry is responsible for implementation of the Basic Law. The SMI Bureau is expected to gather general information on the status and development of the SMI sector and to assist in the formulation of government policies. The Bureau also monitors the performance of the specialized institutions, both technical and financial which cater to the needs of the sector. In practice, the limited staff of the SMI Bureau and the fact that SMIB and CNB are supervised by the Ministry of Finance has substantially constrained the efficiency of the Bureau in its efforts to coordinate the delivery of technical and financial assistance to SMI. In order to alleviate these shortcomings, new legislation was enacted in late 1978. The Small and Medium Industry Promotion Law provides for the establishment of a Small and Medium Industry Promotion Corporation (SMIPC) as an independent government entity in charge of promoting the modernization of SMI operations and of supporting SMI cooperative projects.

2.14 The Small and Medium Industry Promotion Corporation. Established in January 1979, SMIPC operates under the direct supervision of the SMI Bureau of the Ministry of Commerce and Industry. Over time, the Government expects SMIPC to develop into a powerful national agency in charge of implementing policies for the development of the SMI sector. SMIPC can therefore be expected to develop gradually its capability to supervise and coordinate the delivery of technical and financial assistance to SMI by the various specialized agencies. At present, however, SMIPC still is a very young institution with limited capabilities. SMIPC's major activities cover (a) financing and implementing the modernization of specific SMI projects in priority sectors as defined by MCI; (b) financing and implementing such cooperative activities as industrial estates and common processing facilities; (c) delivery of managerial and technological assistance through on-site extension services and staff training; and (d) research and publication of data on the SMI sector as a whole and on specific industrial subsectors.

2.15 In order to carry out these functions, SMIPC has recruited capable professionals, mostly with an engineering background, and has been able to offer a very competitive salary scale relative to other government institutions. Its total staff reached 151 at end October 1979 of which about 100 were professionals. Recruitment of about 50 more engineers is planned for 1980. Government expectations from the establishment of SMIPC can be measured by the size of the financial resources made available to it mainly from annual budgetary resources. These resources /1 reached W 26.5 billion

/1 Called the SMI Promotion Fund.

in 1979 and comprised (i) W 15.7 billion /1 in funds loanable to individual SMI projects through SMIB; (ii) W 5.5 billion for cooperative and industrial estate projects; (iii) W 1.6 billion for administrative expenses; and (iv) W 3.7 billion for extension services and training. Total resources available to SMIPC in 1980 as Promotion Fund are expected to reach W 31.3 billion, including W 16.5 billion in loanable funds. The use of loanable resources available from the Promotion Fund is restricted in the Enforcement Decree of the SMI Promotion Act to enterprises employing more than 50 workers and having assets of more than W 100 million. The upper limit of 300 workers normally applicable to SMI enterprises has been raised for specific industries to 500 workers.

2.16 Korea Federation of Small Business (KFSB). Established in 1962 in accordance with the SMI Cooperative Act, the Federation is the apex institution for SMI provincial and national cooperatives. At end-July 1979, 16,100 SMI firms held membership in one of the 181 cooperatives controlled by the Federation. The main activities of the Federation comprise joint purchases and sales to member enterprises, delivery of technical and managerial assistance and compilation of data and surveys of the SMI sector as a whole.

2.17 Promotion of Rural Industries. Beginning in the early 1970s, the Government has been placing greater emphasis on the creation of off-farm employment. The Saemaeul Program incorporates various elements including one directed at the establishment of SMI projects in rural areas. By end August 1979, a total of 651 factories had been identified as Saemaeul projects and 509 had been completed. Total employment creation was estimated at about 70,000. For 1980, establishment of 100 new Saemaeul factories is being planned.

2.18 In addition to the Saemaeul Program, the Government has been encouraging a better regional dispersal of industries by sponsoring and financing industrial estates reserved for SMI. By end-1978, there were 11 such estates operating in Korea. SMIPC is now expected to take the lead in planning and establishing new industrial estates and common processing facilities for SMI. To increase its effectiveness, SMIPC has recently proposed to the Government a revision of the cumbersome and ineffective legislation currently applying to the establishment of industrial estates.

2.19 Other Programs. The Government has launched a number of programs aimed at supporting specific objectives and activities within the SMI sector. The 1975 SMI-Affiliation Law aims at promoting linkages between large and smaller enterprises. So far, 37 large enterprises have established

/1 W 15.4 billion for working capital and W 0.3 billion for equipment purchases.

such relations with some 157 SMI units operating in 5 industrial activities. Firm contracts subject to government approval and control must be established between large firms and their suppliers. In addition, the Government has reserved 23 activities /1 for SMI firms only. In 1976, the Government also initiated a program of assistance to SMI machinery producers. Five hundred enterprises would be selected from priority sub-sectors between 1976 and 1981; by end 1978, 200 had been identified.

2.20 An area in which government programs have not been very successful is technical and managerial assistance. In 1979, the Ministry of Commerce and Industry had accredited seven institutions /2 which were expected to deliver on-site guidance and provide training to the workers of SMI enterprises. A total of 3,335 firms were expected to receive on-site guidance. The number of firms to be assisted ranged from 5 for CNB to 2,200 for the Chamber of Industry. By end-August 1979, no more than 860 had actually been assisted. Several of the agencies expected to assist SMI enterprises are not equipped to do so efficiently. Most of them cater to a particular segment of the SMI sector and duplication is almost inevitable. It seems that an urgent task of reorganization and coordination needs to be undertaken by the Government in the area of technical assistance to SMI.

Financial Institutions Supporting SMI

2.21 Financial assistance programs are discussed in para. 2.19. The institutional framework for the delivery of financial assistance to the SMI sector comprises SMIB, CNB and the Korea Credit Guarantee Fund (KCGF). In addition to these institutions which specialize in assisting the SMI sector, /3 the commercial banks also provide a large proportion of the financial resources, albeit mostly short-term, to Korean SMI.

2.22 The Small and Medium Industry Bank (SMIB). Established in 1961, SMIB is a government-owned institution /4 geared specifically to meet the financial and to a lesser extent technical assistance requirements of SMI. Its mandate encompasses assistance to entrepreneurs employing 5 to 300 employees. SMIB's total loan portfolio reached W 457 billion (US\$942 million)

/1 Such as knitted toys and printing.

/2 Comprising the Industry Advancement Administration of the Ministry of Commerce and Industry, SMIPC, the Korea Federation of Small Business, the Korea Chamber of Commerce and Industry, the Korea Credit Guarantee Fund, CNB, and SMIB.

/3 Except for KCGF which also issues guarantees for large-scale priority industries (45% of outstanding guarantees).

/4 The Government owns 99.9% of SMIB's share capital.

at end-1978 and SMIB's clientele comprised 17,000 of the 27,000 SMI enterprises in the manufacturing sector. The Government has recently authorized an increase in SMIB's authorized share capital from W 30 billion to W 100 billion in order to allow a further expansion of its lending operations. SMIB's disbursements of term loans for equipment financing reached about US\$195 million in 1978 of which about 54% was in foreign exchange. On average, approximately 46% of SMIB's total term lending over the period 1976-78 has gone to the SSI sector defined as enterprises employing up to 100 workers. SMIB's long-term lending to the SSI sector reached W 35 billion in 1978 compared to W 17.1 billion for CNB.

2.23 The Citizens National Bank (CNB). Established in 1962, CNB has been very successful in attracting deposits from small savers. Its total deposits reached W 1,010 billion at end-September 1979. Its loan portfolio, short- and long-term, reached W 523 billion or 52% at the same date because of restrictions imposed by MOF on its lending operations. CNB's total loan disbursements reached W 341 billion in 1978 of which W 170 million (50%) was for SSI and the balance for consumer financing. Of CNB's total SSI lending, about 10% was in the form of term loans (subject to a maximum maturity of five years). In 1979, CNB received a foreign currency loan of US\$10 million from ADB. These resources as well as the proposed US\$30 million Bank loan would enable CNB to cover partly the existing gap between demand and supply of foreign currency resources in the SSI sector.

2.24 Korea Credit Guarantee Fund (KCGF). Formerly operated by SMIB, the KCGF became an independent institution in 1976. The KCGF is authorized to issue guarantees with a maximum outstanding amount of 15 times its share capital which reached W 96.2 billion at end-July 1979. Total outstanding guarantees reached W 543 billion at that date with 52% extended to SMI enterprises.^{/1} About 80% of KCGF guarantees are for working capital loans. Average guarantee size reached W 26 million in 1978. Separate figures for SSI industries are not available. Eighty percent of KCGF's share capital at end-1978 came from annual remittances from deposit money banks equivalent to 0.5% of their outstanding loan portfolio. The balance consisted primarily of retained earnings. KCGF charges an annual fee of 1% on loan guarantees payable by the subborrower. Guarantee coverage by KCGF is limited to W 1 billion for large industrial and W 500 million for SMI. Guarantees are available for projects with insufficient collateral; the KCGF is not expected to give any guarantee coverage on the basis of risk.

^{/1} The KCGF Act stipulates that at least 40% of guarantees outstanding should be for the SMI sector.

Flow of Funds to SMI

2.25 The Korean SMI sector receives direct financial support from (a) the commercial banks (nationwide and local banks); (b) the Small and Medium Industry Bank; and (c) the Citizens National Bank. The following table shows a breakdown by source of funds of SMI loans outstanding over the period 1976-November 30, 1979.

LOANS OUTSTANDING TO SMI SECTOR
(in W billion)

	<u>1976</u>		<u>1977</u>		<u>1978</u>		<u>1979</u>	
	Amount	%	Amount	%	Amount	%	Amount	%
Nationwide banks	437.5	45	632.3	48	908.6	48	1,295.4	50
Local banks	146.4	15	204.8	15	273.0	15	358.3	14
SMIB	225.4	23	296.5	22	456.9	24	613.9	24
CNB	166.5	17	193.4	15	237.5	13	305.2	12
<u>Total</u>	<u>975.8</u>	<u>100</u>	<u>1,327.0</u>	<u>100</u>	<u>1,876.0</u>	<u>100</u>	<u>2,572.8</u>	<u>100</u>

It is apparent from the above table that commercial banks represent the major source of financial support for SMI with nearly two-thirds of the total SMI portfolio. To a large extent, this results from a BOK requirement that SMI lending account for 30% of the loan portfolio of nationwide banks.^{/1} Most of these loans however are short-term. The lending rate applicable to these loans is the standard rate of 18.5% p.a. for loans under three years and 19.5% over three years. SMIB has been able over the period 1976/77 to maintain a 22-24% share of outstanding SMI loans. It is estimated that approximately 45% of its loans were extended to small enterprises employing less than 100 persons and 55% to medium sized ventures.

2.26 CNB's share in total SMI lending has been declining regularly over the past three years to a point where its outstanding SSI portfolio barely exceeds the estimated SSI component of SMIB's portfolio. This is primarily due to the very tight credit ceilings imposed by MOF on CNB's lending operations. These ceilings effectively prevent CNB from using for lending purposes all the resources it mobilizes from depositors.

2.27 An important feature of SMI lending is that contrary to other directed lending programs undertaken by financial institutions at the

^{/1} 40% in the case of local banks.

request of the Government, only a minor portion can be considered as subsidized credit. Net increases in SMI lending operations had been projected by BOK at W 300 billion for 1979. Of this total, the subsidized SMI Low Interest Fund channelled by SMIB at 15% p.a. amounted to W 60 billion or 20%. In addition, SMIB has been operating since early 1979 as the lending channel for the SMI Promotion Fund /1 (para. 2.14) whose proceeds are lent to borrowers at rates of 10% to 15% with a 2% spread accruing to SMIB.

3. THE FINANCIAL SECTOR

Financing Long-Term Capital Investment

3.01 In spite of some recourse to rolling over of short-term borrowings by and large Korean enterprises except for the SSI sector have had reasonable access to long-term resources /2 to finance their investments. These resources comprise internally generated funds, including additional equity financing from shareholders and external resources, i.e. borrowings. BOK surveys of fund flow statements of manufacturing enterprises and other studies of investment patterns in Korea suggest that internally generated funds account for as much as 50% of GDCF in the SSI sector and about 40% for larger firms. It can be inferred from these studies that, on average, self-financing accounts for about 45% of manufacturing GDCF. External sources which comprise both domestic institutional sources (bank and nonbank) and noninstitutional sources (capital markets, direct borrowings from abroad and the UMM) provide the 55% balance of GDCF. Based on current price GDCF, total financial resources raised externally by Korean manufacturing enterprises in 1978 could be estimated at W 850 billion.

3.02 Findings of the Financial Sector Mission, which visited Korea in November 1979, show that in 1978 institutional sources of funds in Korea provided incremental long-term resources aggregating W 591 billion; this represented 67% of total resources mobilized externally for financing manufacturing investment. Noninstitutional sources provided the remaining W 259 billion. Among these, corporate debentures issued on the capital market provided more than half.

3.03 The above figures indicate that institutional sources of funds are the second largest source of long-term funds for the manufacturing sector after self-financing. This role has been growing in importance over the past few years; annual increments in outstanding term loans of financial

/1 W 15.7 billion in 1979.

/2 i.e. resources whose maturity exceeds one year.

institutions to the manufacturing sector have grown at an average annual rate of 50% over the period 1976-78, compared to a growth in manufacturing GDCF of 42% p.a. As a result, increments in term loans outstanding which accounted for 29% of manufacturing GDCF in 1975 reached 38% in 1978.

3.04 A tremendous expansion was also recorded in the corporate bond market. The volume of funds raised by placement of debentures on the securities market has grown by an average of 95% p.a. over the 1975-78 period. Corporate bond issues by manufacturing sector firms reached nearly W 241 billion in 1978 /1 compared to W 32 billion in 1975.

Financing Short-Term Requirements

3.05 The supply of long-term resources represents only part of the support which institutional sources of funds provide to the manufacturing sector. Manufacturing firms rely primarily on financial institutions, including short term finance companies, for the supply of short-term resources to cover their working capital requirements. Other sources of funds are practically limited to the unorganized money market. As a consequence, short-term lending operations represent a major part of the portfolio of Korean financial institutions./2 Over the period 1976-78, short-term operations accounted for 66% of the increases in the total outstanding portfolio of financial institutions /3 and increments in the outstanding short-term portfolio of financial institutions have grown at an average of 59% p.a., faster than the 50% growth in term lending.

Institutional Sources of Funds

3.06 The institutional set-up of the Korean financial sector can be divided into banking (or monetary) institutions which accept deposits from the general public and nonbank financial institutions. Banking institutions are also called "deposit money banks" (DMBs); they comprise conventional commercial banks including branches of foreign banks and six specialized banks./4

/1 Part of the new issues however aimed at replacing maturings debentures.

/1 Except for KDFC and insurance companies which specializes in long-term lending operations.

/2 And 86% of the aggregate portfolio of commercial banks.

/3 The Korean Exchange Bank for foreign trade; the Small and Medium Industry Bank for SMI; the Citizens National Bank for consumer finance and SSI; the Korea Housing Bank for housing finance; the National Agricultural Corporation Federation for agricultural credits and the National Fisheries Cooperative.

The operations of commercial banks are directly supervised by the Bank of Korea (BOK) while specialized banks are under the control of the Ministry of Finance (MOF).

3.07 Over the period 1975-78, some deepening of the financial sector has taken place with the growing importance of nonbanking institutions. The share of nonbank financial institutions in the total gross assets of the financial sector reached 27% in 1978 compared to 23% in 1975. This sign of maturing notwithstanding, the banking system still accounted for 73% of the sector's total assets in 1978 and BOK and the commercial banks together accounted for 50% of total assets in the financial sector.

Deposit Money Banks

3.08 The Commercial Banks. The commercial banking sector in Korea comprises: (a) five Government controlled commercial banks with a nationwide network of branches; (b) ten banks with operations localized in each province; and (c) branches of foreign commercial banks. In aggregate, the assets of commercial banks accounted for 36.9% of the total assets of the financial sector in 1978 down from 37.7% in 1975; this component ratio could be broken down into 30.1% for the five nationwide banks, 4.1% for the ten regional banks and 2.7% for branches of foreign banks. The commercial banking group remains by far the largest source of funds of the manufacturing sector, but its importance has been slowly declining over time. The commercial banks accounted for 65% of the increase in outstanding loans to the manufacturing sector during 1978 compared to 73% in 1974. Their operations, however, are heavily skewed towards short-term lending. In 1978, short-term loans reached close to 90% of the increase in the total commercial bank portfolio. In the same year, the commercial banks supplied only 21% of the increase in the aggregate long-term portfolio of the financial sector as a whole. By comparison, the Korea Development Bank (KDB), which is the largest nonbank financial institution in Korea, accounted for 33%.

3.09 Deposits represent the major source of funds of commercial banks. In 1978, demand and savings deposits together accounted for 54.3% of their total aggregate liabilities (including equity). This ratio actually was substantially lower than the 71.1% reached in 1970. Demand deposits have marginally increased their share of total resources to 21.4% but time and savings deposits have declined regularly from 52.4% in 1970 to 32.9% in 1978. This sharp decline can be related to the 1972 reduction in interest rates and the resulting negative real deposit rates.

3.10 Specialized Banks. The six specialized banks were established by the Government in the early 1960s to service particular economic sectors. Their aggregate assets accounted for 22.8% of the total assets of the financial sector in 1978 down from 23.6% in 1975. The Korea Exchange Bank, which was established in 1967 to take over the commercial foreign

exchange transactions of BOK, accounts for more than half the total assets of specialized banks. Demand and savings deposits represent the main source of funds of specialized banks and accounted for 56% of their total liabilities and equity at mid-1978.

Nonbank Financial Intermediaries

3.11 The declining share of the monetary system, i.e., specialized banks, commercial banks, and BOK /1 in the total assets of the financial sector reflects a certain deepening of the sector linked to the growing importance of nonbank financial institutions. The average annual growth rate of the assets of nonbank financial institutions, reached 24% in real terms over the period 1975-78 compared to an average of 17.3% for the financial sector as a whole. Their share of total assets therefore increased from 23.2% in 1975 to 27.1% in 1978. Nonbank financial intermediaries comprise: (a) four development banks /2 of which the Korea Development Bank (KDB) is by far the largest; (b) the trust account of the Bank of Seoul and Trust; (c) life and nonlife insurance companies; (d) short-term finance companies (STFC); (e) mutual savings and finance companies; (f) postal savings accounts; and (g) securities firms. Out of the seven types of nonbank intermediaries, development banks constitute the largest group as they account for 64% of total assets of nonbank intermediaries.

3.12 The Bank Group is associated with the two development banks active in the industrial sector: KDB and the Korea Development Finance Corporation (KDFC). /3 KDB is the single largest financial institution in Korea. As the principal agent of government financing programs in the industrial sector, it deals primarily with large public and private sector enterprises. Because of the relatively large share of power and transportation projects in its portfolio, the manufacturing sector accounted for 40% of all loans outstanding at end-1978, a lower proportion than for other Korean financial institutions. The privately-owned KDFC also finances relatively large industrial enterprises. Its clientele is restricted to the private sector and until now it has been providing almost exclusively long-term resources

/1 BOK's share of financial sector assets declined from 15.5% in 1975 to 13.2% in 1978.

/2 The Korea Development Bank; the Korea Development Finance Corporation; the Korea Export-Import Bank; and the Land Bank.

/3 The Bank has also made three loans available to SMIB and is proposing that a first loan be considered for CNB. Both institutions are considered as deposit money banks because they accept deposits from the general public. A relatively large part of their operations is, in fact, development financing.

in foreign currencies. In response to rising demands for domestic currency financing, KDFC is in the process of being converted into a long-term credit bank which should, inter alia, ensure its access to larger amounts of long-term domestic currency resources.

Noninstitutional Sources of Funds

3.13 Noninstitutional sources of funds include the unorganized money market (UMM) which is primarily a source of short-term resources. Estimates of the importance of the UMM are made difficult by the very nature of transactions and by the fact that a substantial part of the lending operations of short-term finance companies actually represent "recycled" UMM resources. Medium-term suppliers' or buyers' credits have been a substantial source of funds for Korean industries. These direct borrowings from abroad might actually be considered as an institutional source of funds since their availability is usually dependent upon a counterguarantee from a local bank.

3.14 Other noninstitutional sources of funds comprise direct foreign equity investments and the domestic securities market. Direct foreign investments are restricted by the Government to specific sectors and reached about US\$77 million in 1978. The stock and bond markets, particularly the latter, have developed over the past few years into a major source of funds for the manufacturing sector. The importance of the stock market as a source of term finance has fluctuated during the 1970s. Stock market activity expanded rapidly through the mid-70s as a result of government incentives to induce firms to go public. The main incentive was in the form of a 13% tax differential which has been reduced to 5% since 1978. New listings increased by 10% only in 1978 and no new listings were registered in 1979. Trading declined and the stock price index plummeted from 202.8 at end-1978 to 178.2 as of September 30, 1979. Funds raised by manufacturing enterprises on the stock market reached about W 141.1 billion in 1978.

3.15 Since 1977, the corporate bond market has been supplying more resources to the manufacturing sector than the stock market. In 1978, the sale of bonds reached US\$497 million compared to US\$55 million in 1974. The effective yield of bonds varies from 25.5 to 27.4% for a 1-3 year maturity. The rapid growth of the bond market is to a large extent due to the favorable tax treatment granted to buyers for income derived from the purchase of bonds.

Government Control and Direction

3.16 The operations of the financial sector in Korea are characterized by close Government control on the institutions themselves and on their allocation of funds. The Government directly owns controlling participations in the share capital of four of the five nationwide commercial banks and indirectly controls the fifth one. The Government also has majority holdings in the specialized banks and is in full control of the Korea

Development Bank. The top management of these institutions is usually appointed directly by the highest authority under recommendation by the Minister of Finance.

3.17 Directed Credit. Government controls are most pervasive in the area of fund allocation. The Government through the BOK and MOF manages a system of "directed" lending, whereby funds are allocated to specific priority sectors, subsectors or individual project enterprises in line with macro-economic objectives. The financial intermediaries are the implementing agencies of this directed lending program.

3.18 The selective credit programs include the support of export activities as the highest priority, the restructuring of the industrial sector with emphasis on heavy and chemical industries and assistance to smaller manufacturing enterprises. These lending programs are channelled through the deposit money banks, primarily the commercial banks, and through KDB. They are made available to borrowers primarily in the form of short-term credits for export loans and medium- to long-term credits for other types of directed lending. There is increasing doubt about the adequacy of maintaining the rigid system of directed lending in Korea because of the growing complexity of the economy and the resulting need for responsive fine tuning. There is no question however that this system has largely contributed in the past to the phenomenal growth and transformation of the industrial sector.

3.19 Subsidized Credit. An important feature of directed credits is the interest rate subsidy attached to most of these loans, a notable exception being the SMI loans of commercial banks. Prior to January 12, 1980, loans for export were generally available at 9% p.a. Equipment loans carried a rate of 15% to 16% compared to a standard rate of 18.5% to 20.5%. Export credit accounted for 62% of all subsidized loans outstanding with deposit money banks at end-1978. KDB handles primarily subsidized loans funded from the National Investment Fund (NIF). These loans accounted for 46% of KDB's total lending to the manufacturing sector in 1978. Including other types of selective credits, 67.6% of KDB's lending in 1978 was in the form of subsidized loans. By comparison, subsidized lending by deposit money banks accounted for 40% of their manufacturing loan portfolio at end-1978.

3.20 Close to 72% of subsidized credits outstanding with deposit money banks at end-1978 were funded from their own resources but were re-discountable with BOK. Government funded programs represented 8% and NIF resources /1 20%. In spite of the negative spread between the average cost of deposit resources and the lending rate for export loans, the profitability of commercial banks is not overly affected since these loans can be rediscounted with BOK with a 5% positive spread for 80% of their value.

/1 Which originate primarily from deposits earmarked by DMBs for the purchase NIF bonds.

Lending Rates and Inflation

3.21 The system of subsidized lending described above aims at (a) improving the competitiveness of Korean exports; and (b) improving financial returns to potential investors in economically desirable projects. The efficacy of this system of subsidized lending is being increasingly questioned, not only because of the negative interest spreads accruing to the financial sector as a whole in view of the higher costs of deposits but also because of potential misallocations of funds. Criticism has also been voiced about the inability of the financial sector to improve the level of national savings primarily because of negative real interest rates on deposits. In order to restore the savings ratio to its 1969-73 level of 21-23% of GNP, it is argued that a 5% premium over the expected rate of inflation is desirable. In January 1980 the Government raised interest rates sharply (the prime lending rate, for example, rose from 18.5% to 24.5%) on both deposits and loans. The new interest rate structure (Annex 4), apart from its anti-inflationary objective, is expected to enable the banking institutions in Korea to achieve better results in their efforts to mobilize savings.

4. THE CITIZENS NATIONAL BANK

A. INSTITUTIONAL ASPECTS

Legal Framework and Ownership

4.01 The Citizens National Bank (CNB) was set up in December 1962 under the Citizens National Bank Act and started its business operations in February 1963. CNB itself evolved from the National Citizen Bank of Korea (NCBK) which was established in 1962 by consolidating a number of small mutual finance institutions dealing with petty finance. NCBK was converted into CNB so as to set up a broad-based financial institution within the framework of government policies to meet the financial needs of consumers and small businesses, while at the same time attracting small household savings as part of a national effort to raise domestic capital for economic development. The CNB Act governs CNB's broad operating policy, scope of operations, administration and capitalization. Under the Act, CNB is empowered to carry out all activities normally carried out by a commercial bank and it also has the unique authority to operate a Mutual Installment Savings and Remuneration Scheme. The Act is supplemented by an Enforcement Decree, Articles of Incorporation and internal regulations. The Act has been amended several times, most recently in December 1977 when CNB's authorized share capital was increased from W 5 billion to W 30 billion, and CNB was authorized to borrow and lend in foreign currencies.

/1 Which originate primarily from deposits earmarked by DMBs for the purchase NIF bonds.

4.02 The Government is the major shareholder in CNB. At September 30, 1979 the Government held 65.6% of CNB's paid-in capital of W 5 billion;^{/1} 5 nationwide commercial banks, also owned mainly by the Government, held a further 34.1%, with the remaining 0.3% held by private interests (see Annex 5).

4.03 Under the CNB Act, the senior management of CNB (President, Deputy President, Auditor and Directors) are appointed by the Government which must also approve CNB's Annual Operational Plan. In broad policy matters, CNB is under the supervision of the MOF whose approval is required for establishing branches, altering the Articles of Incorporation, suspending business or merging with another institution. As a banking institution, CNB is further subject to supervision by the Bank of Korea, particularly concerning its commercial banking activities including deposit mobilization, bill discounting, and liquidity ratios, all of which are regulated by the General Banking Act. Within this broad supervisory framework, CNB's management is independent in its conduct of CNB's operations.

Management and Organization

4.04 The management of CNB rests with a full-time Board of Directors comprising the President, Deputy President, five Directors and an Auditor. The normal term of office for directors is three years with directors being eligible for reelection. The President, Mr. Jin Wook Chung, has spent most of his career at CNB and was appointed President in May 1979. The Deputy President, Mr. Chul Soon Yun and the five directors have, collectively, many years' experience, mainly in CNB (see Annex 6). Each director is responsible for at least three of CNB's 20 departments (see Organization Chart, Annex 7). CNB has an experienced and professional body of managers and deputy managers in its departments and branch offices. Each branch manager, department manager, director and the deputy president has an authorized ceiling below which he can approve loans; loans above the ceiling are referred to a higher level, with large loans ultimately being approved by the President.

4.05 CNB's major deposit-taking and lending operations are handled through a wide network of branches (divided into main branches, subbranches and deposit offices), with Seoul head office departments responsible mainly for staff activities, such as research, personnel, planning and overall policy, and operating guidelines and supervision of the branches. At September 30, 1979, CNB had 163 branches spread throughout Korea (see Map); of these 81 were in Seoul metropolitan area. Current plans call for an increase to 188 branches by the end of 1981. Due to the size of Busan, a special office called the "Busan Area Activity Promotion Department" supervises and coordinates the activities of the 8 branches in Gyung-sang Nam Do as well as

^{/1} CNB's paid-in share capital was increased to W 30 billion as of December 31, 1979.

the 16 branches in the Busan metropolitan area. No similar arrangement is necessary for Seoul, because the Head Office is in a position to exercise daily supervision of the Seoul branches.

Organization for Term Lending

4.06 The International Department was set up in October 1978 to handle foreign currency borrowing and lending and is the department responsible for the proposed loan. While the International Department will be responsible for the lending of foreign exchange funds, term lending in domestic currency will still remain under the Loan Administration Department. This will mean that the term lending will come under the supervision of two directors. This is unlikely to cause problems in the short term, given the relatively small size of the foreign exchange operations. However, as these operations grow, and as it becomes more necessary to combine domestic and foreign currencies as part of single loan packages, increasing problems of coordination will arise in loan processing. CNB should, therefore, try to find ways to coordinate its lending. A logical step would be the formation of a loan committee with the participation of responsible departments to review together the term loans from the respective departments. Such a committee will enable CNB to maintain uniform criteria in its term lending operations and a bank-wide improvement of project appraisal skills can be achieved. CNB's management is actively considering this idea. As a first step to strengthen the coordination between different departments, the International Department is asked to conduct a preliminary review of all domestic currency term loan applications and its recommendations will be taken into account by the Loan Administration Department.

Staff

4.07 CNB's total staff numbered 6,424 at September 30, 1979 (Annex 8). Of these, 1,340 were classified as professional staff, including 300 financial analysts/accountants, 186 economists/market analysts, 204 lawyers, 7 engineers and 643 general bankers (classified mainly by educational background). Of the total staff, 5,490 or 85%, were in the branches, reflecting their role in collecting deposits and making loans. Total staff requirements are expected to increase at around 8% per year over the next few years, as CNB's operations continue to grow. Staff are usually recruited directly from high school and university, and staff members tend to see CNB as a long-term career source of employment. Staff turnover is consequently low with the professional staff turnover varying between 3.9% and 5.9% during 1975-78. Salary levels at CNB are the same as at other Government-owned banks. Promotion is based on an efficiency rating system derived from seniority, supervisors' annual assessments, and achievements in training seminars.

4.08 The International Department had 41 staff members at November 30, 1979 (Annex 9). Of these, 20 were professionals with training in financial analysis, business administration and economics. Twelve of these staff will

be involved in the processing of long-term foreign exchange loans, including the proposed Bank Loan, with the rest handling the ordinary foreign exchange services. These staff will be supplemented by 9 engineers recruited in early 1979 by CNB into the Credit Analysis Department. These engineers all have substantial working experience and held senior engineering positions in Government and private industry prior to being recruited by CNB. The staff involved in foreign currency lending is of adequate size and qualifications to handle the expected volume of foreign currency lending operations in the near term. CNB intends to further expand the staff of the International Department and relevant staff involved in term lending, as necessary to cope with the future workload. The International Department has high prestige in CNB and the management was able to select from the best available candidates. CNB has worked out a comprehensive training program for 1980 addressed to training the new staff and upgrading the capabilities of the existing one (para. 4.09).

Training

4.09 CNB's Training Department is responsible for co-ordinating a large number of training programs. These programs include in-house training and external courses, mainly through the Bankers Association of Korea. In addition, senior staff members attend courses overseas. In 1978, 2,706 staff members attended 43 in-house courses, 726 attended 106 external courses, and 27 staff members went overseas for periods ranging from 1 to 12 months.

4.10 Because of CNB's primary functions, its staff training has traditionally been oriented towards commercial banking operations and organizational development within CNB. However, the movement into long-term foreign exchange lending has brought about a need for increased expertise in development banking, including project promotion, appraisal and supervision. To fill this need, CNB has developed a comprehensive training program, in association with the KDB and SMIB. Senior officers of KDB and SMIB gave a two-month training course in March/April 1979 to all CNB staff involved in foreign exchange financing. This course encompassed one month of classroom instruction on lending procedures, project appraisal and supervision, and procurement, following by one month of case studies taken from projects previously financed by SMIB. While this comprehensive training has prepared continue its efforts both to train the new staff needed as foreign exchange lending increases, and to acquaint more fully other staff members (in the head office and branches) involved in term lending with appropriate loan processing techniques. Realizing this need, CNB has worked out a comprehensive training program for 1980. Under this program, a higher priority has been assigned to the training of the staff of the International Department and those involved in domestic currency term-loan operations. In order to upgrade the staff's expertise in project appraisal and supervision, a selected number of them will be sent to the Korean Banking Training Institute, the Korea Correspondence College and graduate schools for further training. About 30 staff members are scheduled to be trained overseas in dealing with international banking business, which includes foreign exchange operations, project the staff to handle long-term project financing, CNB will still need to

appraisal and supervision, and procurement procedures. CNB also plans, wherever possible, to send senior staff to attend conferences and seminars to broaden their knowledge of the development banking operations.

Operating Policies and Development Strategy

4.11 CNB has drawn up a Policy Statement to supplement the broad policy and operational guidelines of the CNB Act (Annex 10). It outlines the major policy measures through which CNB intends to assist the development of small industry in Korea. It states that CNB will assist small industry through financial and managerial assistance, with broad priority being given to exporting industries, industries with high employment potential, and those helping to develop technical expertise and product innovation. The policy statement further outlines CNB's general operating procedures, financial exposure limits and provisions for doubtful loans. The financial guidelines do not specify a statutory limit on CNB's long-term debt/equity ratio, but a limit of 7:1 has been agreed with ADB and the Bank agrees with this limit.

4.12 To further emphasize its immediate and specific development objectives, CNB envisages adopting a Development Strategy for the next two years, 1980-81, which outlines specific areas on which CNB intends to place greater emphasis. CNB will make special efforts to assist small and export-oriented projects and those located in provincial areas, to raise long-term resources, to strengthen its research capability and to intensify training of its staff to cope with its expanded operations.

Project Appraisal and Supervision

4.13 CNB's appraisal of its existing domestic currency loans is commercially oriented and relies heavily on the credit standing of the borrower and on collateral security. For the foreign currency term loans financed through the International Department, however, a comprehensive appraisal based on a project analysis has been introduced. The financial, managerial, marketing, and economic aspects of appraisal are carried out by International Department staff, while the technical analysis is undertaken by engineers from the Credit Analysis Department. Both Departments are under the supervision of the Director. The staff concerned have been well-trained and have a good understanding of the steps involved in project appraisal. During the initial period, all project appraisal for foreign currency loans will be carried out by the International Department, with branches simply forwarding loan applications. However, as appraisal skills develop, CNB plans to delegate some project appraisal to the branches. These plans will be kept under review by future Bank missions. CNB will prepare full appraisal reports, similar to those prepared by SMIB, for projects above the free limit, and shorter reports for smaller projects. These shorter reports will be based on the Bank's subproject data reporting system. To obtain an adequate picture of the economic impact of CNB's subloans, CNB has agreed to calculate economic rates of return for all subloans above the free limit. In addition the vision of Director Sang Chan Kim, which will minimize coordination problems.

basic economic and sectoral work underlying the project appraisal needs to be strengthened through increasing the economic staff of the Research Department and through more in-depth industry studies carried out by CNB.

4.14 Follow-up of domestic currency loans is currently delegated entirely to branch offices. The branches monitor projects by telephone, mail and plant visits. The good quality of CNB's portfolio reflects the effectiveness of the follow-up work. Supervision of foreign currency loans will, at least initially, be handled mainly by the International Department, with the branches involved only as necessary. The Department plans to collect monthly reports from project sponsors and make regular follow-up visits, normally every six months, to projects to monitor progress. As the amount of foreign lending grows over the next 2 to 3 years, some supervision work may be delegated to the branches.

Procurement and Disbursement

4.15 CNB has prepared a procurement manual outlining its proposed procedures. Procurement will normally be based on competitive bidding with contracts awarded to the lowest priced responsive bid. The procedures for advertising, bidding and contract award are satisfactory. A separate division has been set up in the International Department to handle procurement. Disbursement of the Bank Loan would be made under approved subprojects at the rate of 100% for directly imported equipment or 60% for the cost of locally procured equipment, representing the estimated foreign exchange component.

B. RESOURCE MOBILIZATION, OPERATIONS AND DEVELOPMENTAL IMPACT

CNB's Role in Financing SSIs

4.16 In Korea, there are four specialized financial institutions, namely, KDB, KDFC, SMIB and CNB, which provide development financing assistance to the industrial sector. KDB and KDFC concentrate on financing relatively large firms while SMIB and CNB deal with smaller ones. SMIB finances small- and medium-sized firms either with total assets not exceeding W 500 million or employing less than 300 workers.^{/1} CNB is restricted to enterprises with less

^{/1} 500 workers for selected industries, including automobile parts, electronic apparatus and its parts, photographic goods, pottery and china, toys and transport services.

than 100 employees,^{/1} but there is no separate asset limitation. While SMIB's total commitments in any one single enterprise in whatever form will normally not exceed 25% of its equity,^{/2} CNB's domestic currency lending to single enterprise should not exceed the following maximum limits: W 30 million for equipment loans, W 40 million for working capital loans and W 30 million for guarantees. It is clear that there is some duplication between SMIB and CNB in the provision of finance for SSI but it is partially offset by the counteracting conditions and practices which tend to separate the clientele of the two institutions. These include the 'one-bank' tradition among Korean borrowers (in part due to collateral arrangements), the branch locations of the two institutions and the fact that CNB's borrowers are in most cases its depositors under various deposit schemes, especially the Mutual Installment Savings and Remuneration Scheme. Moreover, the demand for finance by SSIs has been hitherto much higher than supply. As long as this situation continues, as is likely for some time, the operations of these two institutions will probably continue to be largely complementary.

4.17 CNB's lending operations have grown rapidly and its total outstanding loan portfolio reached W 434.0 billion at end-1978,^{/3} which accounted for 4.3% of all short- and long-term credit outstanding from the commercial banking system (all deposit money banks) and the development banks (Annex 3). At the same time, CNB's outstanding equipment loans of W 32.3 billion amounted to 2.4% of all equipment loans from the commercial banking system. Its equipment loan disbursements reached W 17.3 billion in 1977, which was about 12% of total SSI fixed asset formation for that year. In 1978, while the level of disbursements remained almost the same as in 1977, the percentage dropped to around 7% given the sharp increase in the SSI fixed asset formation in 1978.

Resource Mobilization

4.18 CNB has relied almost exclusively on its deposits in financing its lending operations. Apart from ordinary demand and savings deposits, CNB

^{/1} CNB's lending is restricted to small-scale manufacturing, mining and transportation enterprises employing 5 to 100 workers and construction and service enterprises employing 5 to 20 workers. CNB is allowed to lend to enterprises employing more than 100 workers, if the loan amount is limited to W 10 million. (In the first nine months of 1979, 2.5% of CNB's equipment loan approvals went to such enterprises.)

^{/2} As of the end of 1978, SMIB's equity reached W 25.8 billion. Twenty-five percent of its equity amounted to W 6.5 billion. This compared with total CNB's exposure in one enterprise of W 100 million.

^{/3} By September 30, 1979, CNB's total loan portfolio reached W 523.0 billion.

offers a variety of deposit schemes (for a sample, see Annex 4) differentiated by depositor, purpose, and maturities, and by September 30, 1979 it had mobilized deposits totaling W 1,010 billion. The most important deposit scheme is the Mutual Installment Savings and Remuneration Scheme under which CNB and the depositor enter into a contract when the first deposit is made. The depositor undertakes to deposit a fixed amount each month for a specified period (15-60 months). In return, CNB agrees to make a loan (called "remuneration") after 1/5 of the contract period is completed and deposits made as contracted. The loan and deposit amounts are so calculated as to be equal, after inclusion of interest on both sides, at the end of the contract period, when the deposits and the loan are simultaneously liquidated. CNB has the exclusive authority to operate this Scheme in Korea. It also handles Property Formation Deposits to facilitate the purchase of houses by wage earners. Under this Scheme, which started in 1976, wage earners are permitted to deposit up to 30% of their monthly salary in the deposit account, earning a rate of interest up to 27% p.a. CNB receives a subsidy of 9% from the Government and itself pays the remaining 18% to the depositor under the Scheme. CNB is obligated to make a housing loan twice the amount of total deposits under this Scheme. Using its widespread branch network, CNB is able to mobilize savings from small savers, including both individuals and enterprises, very effectively.

4.19 Compared with other development banks in Korea, CNB has relatively limited access to government funds, particularly to long-term domestic currency resources. (CNB has served as an on-lending agent for such government funds as Industrial Rationalization Fund (IRF) and funds for financing war veterans but the amounts are small, W 1.3 billion at September 30, 1979). In view of CNB's role in financing SSI, the Government should allow CNB to have access to the newly established SMI Promotion Fund (an amount of W 15.7 billion has been allocated for this Fund for 1979 and an additional W 16.5 billion for 1980). The appraisal mission has discussed this matter with both the Government and CNB. The Ministry of Commerce and Industry agreed to the proposal that CNB be given access to the funds provided under the SMI Promotion Fund (to which, to date, only SMIB has had access). In March 1980 CNB will be designated as a handling intermediary for the SMI Promotion Fund and an agreement for the management of part of the funds will be executed between CNB and SMIPC. The funds have a maximum maturity of 10 years and the onlending rate is 23.5%.

4.20 CNB's continuing resource mobilization efforts and the credit ceilings imposed by MOF (in consultation with BOK) resulted in a large surplus of liquid funds which are being kept as cash in banks, invested in securities or onlent in the form of deposits with other banks and via the call money market. At September 30, 1979, a total amount of W 364 billion remained in such liquid or semiliquid form, yielding an average interest rate of 13.2% p.a. compared with its average lending rate of around 18.5%. Since CNB's principal role is to assist SSI, channelling of such liquid funds through

the commercial banking system and the call money market, which would in most cases be benefitting large-scale industries, does not appear to be in line with the institution's objectives and, therefore, the credit policy applicable to CNB deserves constant review by the Government. CNB, on its part, is focusing more attention on its resource allocation, seeking ways to reduce the level of its liquid funds. As a departure from its past policy, CNB has decided to make 10-year term loans (so far it only confined to 5-year loans) and an initial amount of W 2 billion has been earmarked by its Board for this purpose for 1980.

Summary of CNB's Lending Operations

4.21 CNB's lending operations are summarized in Annex 12. At end-1978, CNB had a total outstanding loan portfolio of W 434.0 billion, more than double the 1975 level of W 191.9 billion. (By end-September 1979, it stood at W 523.0 billion.) Playing an important role as a popular savings bank, CNB's operations have primarily emphasized resource mobilization, offering a wide variety of deposit schemes to savers. On the lending side, CNB provides three types of financial assistance (in domestic currency): 'general populace' (consumer) loans, short- and medium-term working capital loans and medium-term equipment loans to small industries. CNB is authorized by its Act to extend equipment loans to a maximum of W 30 million, working capital loans to a maximum of W 40 million and guarantees up to W 30 million. The Government is presently considering CNB's request to increase the limit on equipment loans from W 30 million to W 100 million. CNB started in 1979 to provide long-term equipment loans in foreign currency against its resources obtained from ADB. During the four-year period from 1975 to 1978, CNB's overall loan approvals increased from W 123.0 billion to W 340.5 billion, showing an average annual growth of 22.6%. However, for industry loans (including working capital and equipment loans), a decline of 9% was registered in 1978 after growth at an average annual rate of 27.6% in 1975-77. The consumer loan approvals increased at an annual rate of 26.6% in 1975-77 and rose sharply, by 57.6%, in 1978. This stemmed from the fact that the Government started in 1978 to impose credit ceilings on financial institutions and CNB was unable to maintain a proper balance between industry lending and consumer lending because of the compulsory nature of the Mutual Installment Savings and Remuneration Scheme. The industry loan and general populace loan approvals increased, on an annual basis, 19.5% and 18.8% respectively in the first nine months of 1979.

4.22 Equipment Loans. CNB's cumulative equipment loan approvals over the period January 1975-September 1979 amounted to W 57.5 billion. Approvals increased consistently until 1977. In 1978 equipment loan approvals actually declined by 1.4% to W 17.1 billion (from W 17.3 billion in 1977) mainly because of the impact of credit ceilings imposed by MOF starting in

August 1978./¹ Equipment loans have accounted only for an average of 5.2% of total annual approvals over the period. The number of equipment loan approvals increased from 3,903 in 1975 to 5,257 in 1978, and their average size increased from W 2.02 million in 1975 to W 3.25 million in 1978. In the first nine months of 1979, the average size registered further increases to W 3.98 million. At September 30, 1979, 79.1% of CNB's outstanding equipment loans were made under the Mutual Installment Savings and Remuneration Scheme. The Scheme is attractive because it enables the borrower to secure medium-term (up to five years) loans at low interest rates and because it provides CNB with a steady flow of deposits which have been 'contracted' and can therefore be predicted with reasonable accuracy. On the other hand, by virtue of its contractual features which in effect give the depositor the right to borrow, it does not leave CNB with much, if any, flexibility in making independent allocative decisions. Apart from the loans extended under this Scheme, CNB also makes some equipment loans (up to five years maturity) on a more usual basis outside the Scheme, based on project and collateral appraisal. These loans accounted for 21.1% of outstanding equipment loans at September 30, 1979.

4.23 Working Capital Loans. These accounted for 44.9% of total loan approvals in the first nine months of 1979, compared with 59.7% in 1975. At September 30, 1979, outstanding working capital loans amounted to W 257.7 billion which represented 49.3% of the total portfolio. 68.8% of the outstanding working capital loans belong to the Mutual Installment Savings and Remuneration Scheme. The amount of working capital loan approvals declined by 10% in 1978 but the trend was reversed in the first nine months of 1979. Short-term working capital loans are evaluated on a collateral basis.

4.24 General Populace (Consumer) Loans. By number, consumer loans accounted for the overwhelming bulk of total approvals (82.6% in 1978 and 85% in the first nine months of 1979). However, by amount, consumer loans represented only 50% of total approvals in the same periods. The growth in approvals has been rapid, particularly in 1978 which registered an increase of 57.6% over the 1977 level. The upward trend continued in the first nine months of 1979 registering an increase of 19% on an annual basis. This was achieved at the expense of loan approvals for small industry working capital and equipment loans. As of the end of September 1979, 68.1% of the general populace loans were under the Mutual Installment Savings and Remuneration Scheme.

Characteristics of CNB's Equipment Loans

4.25 The characteristics of CNB's equipment loan approvals for 1975-78 and the first nine months of 1979 are summarized in Annex 13.

¹ These are stipulated quarterly and apply to the operations of the institution as a whole (i.e., not specified per loan activity). They are regularly revised on the basis of incremental deposits received by CNB during the previous quarter.

4.26 Sectoral Distribution. The most notable feature of CNB's sectoral allocation is its remarkable stability from 1975 to 1978. The manufacturing sector accounted for the bulk of its equipment loan approvals, increasing slightly from 68.7% in 1975 to 72.9% in 1978. But this pattern was changing in the first nine months of 1979 when the share of the manufacturing sector dropped to 48.4%. This is mainly attributable to the fact that a number of loans were made to finance projects in the transportation sector, increasing its share from an average of 8.6% during 1975-78, to 27.2% in the first nine months of 1979. CNB has no explicit policy on its exposure in individual industries. Textiles took up 21.4% of total approvals in 1978, followed by machinery (11.5%), chemicals (10.3%) and wood products (10.2%). The corresponding percentages dropped to 14.7%, 7.7%, 5.2% and 3.7%, respectively in the first nine months of 1979.

4.27 Geographical Distribution. The geographical pattern has been very stable over the years 1975-78. Its actual distribution remained highly skewed in favor of Seoul, which accounted for 56.9% of total approvals in 1978, with Busan City absorbing a further 7.6%. The combined urban areas of Seoul and Busan accounted for 64.5% of equipment loan approvals in 1978, which proportion decreased slightly to 62.1% in the first nine months of 1979. The recent trend of CNB's operations is therefore not towards greater geographical dispersal. Government policy has, however, encouraged a more even spread of industrial activity for all enterprise size groups, including SSIs which have enjoyed preferential treatment under the Saemaeul Movement and by the establishment of several specialized industrial estates. CNB is prepared to move toward more geographical dispersal, as emphasized in its Development Strategy for 1980-81 (Annex 11).

4.28 Loan Size Distribution. Due to price inflation and changes in Korea's industrial structure, the average size of CNB's equipment loans has increased substantially (Annex 13). In 1975-77, 66.0% of the loans approved were below W 5 million but this declined to 43.5% in 1978 and the first nine months of 1979. Conversely, there were no loan approval in the W 20-30 million range in 1975-76 and only 6.8% in 1977, while this category accounted for 13.1% of the total during the period January 1978 to September 30, 1979. The average size of equipment loan approvals went up from W 2.02 million in 1975 to W 3.25 million in 1978, and to W 3.98 million in the first nine months of 1979.

4.29 Duration of Loans. The maturity of equipment loans approved by CNB has shortened between 1975 and September 30, 1979 (Annex 13). Loans below three years increased from 57.0% to 70.0% over that period, while maturities of three-to-five years declined from 43.0% of total approvals to 30.0%. This is attributable to the fact that in the earlier years CNB made loans of longer maturities under a special government fund and term loans under the Mutual Installment Scheme were usually of shorter duration because of the contractual waiting period. CNB was unable to make loans having maturities longer than five years because of lack of long-term resources.

4.30 Subborrower Employee Size. The most prominent feature of CNB's equipment loan clientele is the large proportion of very small firms. Enterprises with only 5-20 employees received 70.0%-83.1% of CNB's equipment loans in 1975-78 and 58.5% in the first nine months of 1979. The firms employing 50-100 workers have received only 7.0% of CNB's equipment loans since 1975.

4.31 Other Features. The total asset size of CNB's equipment loan borrowers (at the application stage) averaged W 208 million /1 with a substantial proportion below W 150 million. Only about 12% (by number) of CNB's clients exceeded the W 500 million total asset size, specified as one of two alternative definitions of SMIs. Around 20% (by number) of CNB's equipment loans went to limited liability companies in 1978, the other borrowers being single-ownership private enterprises. By type of project, CNB allocated its equipment loans mostly to expansion projects in 1978, accounting for 70% of total loan amount and 72% by number. New projects received 27% (by amount), the remainder going to replacement projects.

4.32 Economic Analysis. CNB has hitherto monitored only partial economic indicators; ERRs (and FRRs) have not been calculated in the past. A sample survey of such partial indicators covering 87 projects before July 1979 is presented in Annex 14. There are a few features worth noting. The proportion of total project cost financed by CNB is fairly low, averaging 35.2%. This is due partly to the general inadequacy of collaterals of CNB's clients and partly to the low ceilings on CNB's maximum equipment loan size. As regards employment creation, the performance of CNB-financed subprojects has been satisfactory. These projects created 806 new jobs of which 247 or 31% were taken by skilled workers. The average investment cost per incremental job was W 3.8 million (US\$7,835) which indicates that CNB has emphasized relatively labor-intensive subprojects.

4.33 CNB's economic evaluation of projects would be greatly strengthened if it included a calculation of ERR's. During negotiations, agreement has been reached that CNB will calculate ERR's for subprojects above the free limit to be financed under the proposed loan.

4.34 Foreign Currency Subloans. The average employee size of applicants for foreign currency term loans under the ADB loan of \$10 million to CNB is 44 workers. This is higher than the average for domestic currency equipment loans. The pipeline of projects to be financed by the ADB loan shows that an amount of US\$6.3 million (out of US\$10 million) may go to clients with less than 50 employees. The average total asset size is W 329 million, with 12 (out of 50) enterprises being larger than the SMI limit of W 500 million total asset size. The average loan size is US\$199,300, with 14 (out of 50) enterprises provisionally receiving US\$300,000, which is the ceiling on subloan

/1 Based on a review of the applications approved during 1978.

size agreed between CNB and ADB. On balance, while the data are preliminary and limited, it seems that the foreign currency loans are going to slightly larger SSIs than are the domestic currency equipment loans.

Other Activities

4.35 Extension Services. Under the SMI Promotion Act, CNB was authorized as one of several institutions to provide extension services to its clients. The assistance hitherto extended by CNB has been carried out mainly at the branch level and is usually provided in connection with a loan application. It has focussed principally on managerial, administrative and bookkeeping matters. This assistance serves to simultaneously improve the business prospects for CNB's clients and therefore also the quality of CNB's portfolio. For 1980, CNB has submitted a plan to the Ministry of Commerce and Industry outlining the extension services (including managerial counseling and technical assistance) to be rendered to about 100 small enterprises, including all borrowers of CNB's foreign currency subloans. This plan is satisfactory to MCI. At the latter's suggestion, CNB will work closely with both SMIB and SMIPC in providing technical assistance to the small firms.

4.36 Promotion Activity. CNB's promotion work is being expanded. It has regularly conducted (in 1970, 1971, 1973 and 1977) a very comprehensive small industry survey which forms part of EPB's National Wealth Survey. This will be continued. CNB also monitors economic developments in the SSI sector. More recently, the Credit Analysis Department of CNB has focussed on active project promotion by undertaking specific industry studies. Their principal objective is to analyze the credit status and trends of enterprises in selected industries in order to generate useful information for CNB's lending operations. This activity should be further strengthened particularly by including engineers in the survey staff. CNB should make full use of its extensive branch network in identifying and developing projects in collaboration with small entrepreneurs scattered in various provinces. In conjunction with its promotion work, CNB has specified a number of lending priorities which currently include export-oriented and subcontracting enterprises. This is in accordance with Government policy.

4.37 Guarantees. CNB provides security guarantees as an agent for the KCGF. It is empowered to issue guarantees, up to a limit of W 20 million,^{/1} beyond which guarantees are subject to prior approval of the KCGF. Credit analysis is undertaken in accordance with KCGF guidelines which are detailed and cover financial, economic and managerial aspects. This type of analysis helps promote a cash-flow business prospects approach to loan evaluation, as opposed to a purely collateral approach. At end-September 1979, CNB had made loans amounting to W 34.9 billion which were covered by credit guarantees.

^{/1} There are several exceptions to this "free limit," for example, W 100 million for defense or export industries, cooperatives, etc.

This accounted for 6.7% of the total outstanding portfolio as of that date. For working capital loans, this was as high as 12.8%, and for equipment loans 7.1%, while for consumer loans it was zero.^{/1} CNB can also issue guarantees for its clients who take loans from other banks.

4.38 Equity Investments. CNB's equity investments are summarized in Annex 15. Legally CNB is not authorized to make equity investments in its clients in accordance with its Act (Article 18). It has, however, made a few small investments in nonclient companies at the suggestion of MOF.^{/2}

At end-September 1979, CNB held investments in 14 companies at an original cost of W 2.05 billion. Dividends received in 1978 were low (W 7.1 million) representing an average yield of 0.35%. All CNB's investments represented small minority shareholdings except for its ownership of the Bukook Mutual Savings and Finance Company in which CNB has invested W 1.5 billion. In this case, CNB's involvement (at the suggestion of MOF) was intended as a rescue attempt and may be terminated once Bukook is profitable again. All equity holdings by CNB are considered temporary investments, putting to use its surplus funds.

C. FINANCIAL POSITION AND PERFORMANCE

Financial Position

4.39 CNB's summarized balance sheets as of December 31, 1975-78 and September 30, 1979 are given in Annex 16. During the period from 1975 to 1978, CNB's total assets had increased more than threefold, from W 263.6 billion (US\$543 million) as of December 31, 1975 to W 868.8 billion (US\$1,791 million) as of December 31, 1978, showing an average annual growth of about 49%. In the first nine months of 1979 a further growth of 28% was registered, bringing the total assets figure to W 1,113.4 billion equivalent to US\$2,295 million. This impressive growth was entirely attributable to the sharp rise in deposits. The growth of short-term deposits was slightly higher than that of medium/long-term deposits. This clearly indicates that CNB's efforts in mobilizing resources from small savers have been very successful. However, CNB's loan portfolio did not show the same growth

^{/1} For total loans outstanding, 80.1% was secured by collateral, 7.3% by credit guarantees and 12.6% was unsecured.

^{/2} As part of MOF's monetary policy operations, CNB has, like other financial institutions, also invested in Monetary Stabilization Bonds (to an amount of W 55 billion outstanding at end-September 1979). This is not, of course, an equity investment.

pattern. Its short- and long-term loans combined increased at a much lower rate, around 31% a year during 1975-78. (At December 31, 1975, CNB's total loan portfolio accounted for 73% of its total assets. By the end of 1978, this ratio had dropped to 50%). Its lending operations have been affected by the credit ceilings imposed by MOF (in consultation with BOK) in August 1978, with subsequent adjustments. The slow growth of its loan portfolio relative to its total assets, also reflects the fact that CNB's resource allocation was not as aggressive as its resource mobilization. As a result, CNB has remained very liquid, with its sizeable liquid funds lent to other domestic banks, or in the form of call loans, or invested in securities. As of December 31, 1978, such liquid funds, including cash, reached W 327.2 billion, equivalent to 75% of its total loan portfolio. As of September 30, 1979, such liquid funds were W 424.5 billion and the ratio went up to 81%.

4.40 CNB has been operating on a very thin equity, which accounted for 1.3% of total liabilities and equity at the end of 1978, showing a debt/equity relationship of 77:1 (40:1 as of September 30, 1979). The long-term debt/equity ratio (after excluding current maturities of long-term debt) reached 24:1 (9:1 as of September 30, 1979). After adjustments by excluding current maturities of long-term debt, BOK's reserve requirement and remunerated installment savings, the long-term debt/equity ratio amounted to 14:1 (5.1 as of September 30, 1979). A long-term debt/equity ratio of 7:1 with the above adjustments has been agreed upon between CNB and ADB, which is also acceptable to the Bank. As of December 31, 1979, CNB has increased its paid-in share capital from W 5 billion to W 30 billion by the end of 1979.^{/1} After this increase, CNB's long-term debt/equity ratio (adjusted) is expected to fall within the range of 5.2:1 to 6.1:1 in the following four years, 1980-83.

4.41 Taking into account all the current maturities of its loans and long-term debt, CNB's current ratio has risen from 1.02 in 1975 to 1.19 in 1978 and again declined to 1.10 as of September 30, 1979. Since a substantial portion of its short-term debt can be counted on to be rolled over, CNB's liquidity position was satisfactory. CNB has agreed with ADB to maintain a current ratio of 1.1:1, which would be acceptable to the Bank. Since CNB has been using a portion of its short-term resources to finance long-term loans, CNB is prepared to adopt appropriate measures to correct any resulting imbalances. It was agreed between CNB and ADB that CNB shall keep the maturities of its deposits (and borrowings) and lendings reasonably matched and the Government has agreed to provide long-term funds to CNB if there should be a serious imbalance between the two in the future.

^{/1} The authorized capital is at present W 30 billion. The net increase in paid-in share capital consisted of W 11.2 billion in cash and W 13.8 billion by way of assets revaluation.

Financial Performance

4.42 Annexes 17 and 18 present CNB's summarized income statements and cash flow statements for the period 1975-78 and the first nine months of 1979. In 1978, CNB's gross income reached W 98.7 billion (W 109.3 billion for the first nine months of 1979), of which 91.5% was derived from interest on all loans. Gross income has increased at an average rate of 46% since 1975, which is satisfactory. CNB's net income stood at W 2,106 million (US\$4.3 million) in 1978, which was more than double that of 1977 (W 1,014 million). In the first nine months of 1979, its net income reached W 2,274 million. In the first nine months of 1979, its net income reached W 2,274 million. CNB's profitability has been very low, with its net profit as a percentage of average total assets hovering within the range between 0.2% and 0.3% during 1975-78. Its return on average equity was more satisfactory. Given its thin equity base, its return increased from around 5% in 1975 to around 20% in 1978 (12% for the first nine months of 1979).

4.43 CNB's low profitability was mainly attributable to its low spread and its high administrative costs. Its spread on "deposits" with other domestic banks has been very low, but such deposits continued to increase. In 1975, such deposits amounted to W 9.7 billion. In 1977-79, the average year-end level reached W 114 billion. In this respect (and via call money operations), CNB acted as a mobilizer of savings which it distributed to various banks which were short of resources. During the process of such resource allocation, CNB was not able to improve its profitability. On the contrary, such operations have contributed to the erosion of its profits gained from normal lending.

4.44 CNB's administrative costs in 1975 accounted for 4.6% of its average total assets. This ratio dropped to a range of 3.6-3.8% in 1976-78, which was much higher than other banks. CNB's extensive branch network and the high overhead costs associated with handling numerous deposit and loan accounts sufficiently explain this situation. Unless CNB's spread is adequately increased across the board, it would be unrealistic to expect CNB to increase its profitability.

4.45 The appropriation of CNB's net profits is subject to the prior approval of MOF. In compliance with its Act, CNB has set aside 25% of its net profit as legal reserves. CNB has paid dividends at 7 to 8% during 1975-78. The remainder of its net profits was accumulated as other reserves. Total reserves of CNB as of December 31, 1978 reached W 6,076 million, corresponding to 1.2 times its paid-in share capital.

Quality of Portfolio

4.46 As of September 30, 1979, CNB's total loan portfolio reached W 522,989 million (US\$1,078 million) consisting of the following types of loans.

	W million	%
<u>Business Loans</u>		
Equipment loans	36,040	6.9
Short-term working capital loans	46,453	8.9
Long-term working capital loans	211,292	40.4
Subtotal	<u>293,785</u>	<u>56.2</u>
<u>General Populace Loans</u>		
Short-term loans	32,965	6.3
Long-term loans	196,239	37.5
Subtotal	<u>229,204</u>	<u>43.8</u>
<u>Total</u>	<u>522,989</u>	<u>100.0</u>

During the period 1975-78, general populace loans had increased at a higher rate than business loans. At the end of 1975, general populace loans accounted for 32% of CNB's entire loan portfolio. This ratio had increased to 45% at the end of 1978 and became 44% at September 30, 1979. Given that CNB has been successful in mobilizing resources from small savers and that it has initiated the mutual installment savings and remuneration and property formation savings schemes, a more rapid expansion of its loans to general populace was a natural development, since depositors were inclined to exercise their options of obtaining loans from CNB.

4.47 The level of arrears on CNB's loans has been low during the past years. At the end of 1975, total arrears accounted for 2.1% of total loans outstanding and loans affected by arrears accounted for 19% of total loans outstanding (Annex 19). These ratios dropped to 1-1.2% and 11-14% respectively during the following three years (1976-78). As of September 30, 1979, arrears/loans ratio dropped further to 0.9%, although a higher percentage (15%) of loans were affected by such arrears. CNB's loan collection ratio averaged about 98% during the period 1975-78, and its loan reschedulings as a percentage of average loan portfolio remained at a low level (1.5%-2.2%) in 1975-77 and went up to 4.2% in 1978. For the first nine months of 1979, the ratio went down to 3.7%. The Government's tight credit policies in 1978 and 1979 have indirectly contributed to liquidity difficulties faced by industries, thus increasing their requests for loan rescheduling.

4.48 Loans written off in 1975-78 averaged W 16 million which was infinitesimal compared with the size of CNB's loan portfolio. This is

explainable by the fact that CNB usually requires a collateral coverage of 120% of its loans. Since real estate contributes the major part of the collaterals, the risk of depreciation in value of the collaterals is minimal.

Provisions Policy

4.49 The Corporate Tax Code in Korea allows banking institutions to make provisions for doubtful loans up to 2% of the loans outstanding.^{/1} Such provisions are exempted from taxation. However, CNB did not take advantage of this stipulation. In 1975 and 1976, CNB did not make any provisions for doubtful loans but simply charged bad debts to its current year's revenue since CNB felt that it had sufficient provisions accumulated in previous years. In 1977, the Credit Guarantee Act required CNB to accumulate special provisions for possible defaults of general livelihood loans at the rate of 0.2% of the total outstanding amount of such loans. Accordingly, CNB set aside W 192 million in 1977. In 1978, the rate of special provisions was raised to 0.5%. (Although CNB is required to accumulate special provisions only on general livelihood loans, it accumulates them on the entire general populace loans). For overall provisions (called ordinary provisions), since 1978, CNB's policy has been guided by the State Audit Board's "Guidelines for Settlement of Accounts by Government Invested Institutions". According to such Guidelines, ordinary provisions for doubtful loans should be made at a rate equal to the rate of actual write-offs on the total loan portfolio during the preceding year. In 1978, CNB allocated W 24 million against its revenue as ordinary provisions and W 710 million as special provisions for doubtful loans and at the end of 1978 total provisions (ordinary and special) stood at W 924 million. According to the Audit Board's guidelines, unutilized ordinary provisions at the end of the year should not be accumulated and should be returned to revenues. CNB has to adhere to such guidelines. In view of the collateral coverage of the CNB's loans and the negligible amounts of actual write-offs in the past, CNB's total provisions in 1977 and 1978 were adequate. Although CNB's provisions policy on special provisions appears to be satisfactory, on ordinary provisions it may become inadequate in future. As CNB starts to make foreign currency loans which will have maturities longer than five years, CNB should formulate a revised provisions policy in anticipation of higher write-offs in the future, and should seek approval of such a policy from the supervisory Government agencies. CNB's past experience with regard to bad debts is no longer a useful guide for its future operations. It needs a policy under which adequate provisions will be made and accumulated for both domestic currency and foreign currency loans. In the meantime, CNB has agreed with the Bank to instruct the external auditors to certify the adequacy of the provisions for doubtful loans based on auditors' review of CNB's portfolio in arrears, its collateral and its future foreign currency loan operations. Based on

^{/1} CNB is exempted from paying corporate income tax on its income. However, it is required to pay defense tax.

auditors' recommendations, CNB will appropriately revise its provisions policy in the near future.

Resource Position

4.50 Details of CNB's resource position as of September 30, 1979 are provided in Annex 20. CNB continued to use a part of its short-term resources to finance its long-term lending operations. As a result, it has not been able to make loans having maturities over 5 years even though adequate demand exists for such loans. At September 30, 1979 its long-term resource short-fall amounted to W 166,458 million, representing 28% of its total long-term lending and investments. This ratio compares with 46% in 1975, 41% in 1976, 36% in 1977 and 33% in 1978. As CNB's long-term lending increased at a much slower pace than its short-term lending (in 1978, the long-term loans outstanding increased 26% while short-term loans increased 163%), the long-term resource gap has become narrower.

4.51 In terms of total short-term resources available, this long-term resource gap accounted for 27%, as of September 30, 1979. This compares with 72% in 1975, 63% in 1976, 47% in 1977 and 39% in 1978. In other words, CNB has been using its resources of less than one year maturity to finance its loans and investments with maturities ranging from two to five years. Given a stable deposit base, with numerous depositors, CNB is not vulnerable to wide gyrations of withdrawals. The present 27% may be considered to fall within prudent limits applicable to CNB's resource utilization. However, this matter should be subject to constant review by the management of CNB and the Government and necessary measures should be taken to avoid any imbalances.

4.52 The overall resource surplus as of September 30, 1979 amounted to W 236.6 billion, equivalent to US\$487.7 million. A fuller utilization of this sizeable excess liquidity also deserves the management's constant attention.

Audit

4.53 In line with the practice of the banking institutions in Korea, CNB has been applying a cash-basis accounting procedure for revenue items and accrual basis for expenditure items. CNB's accounts are audited by the State Audit Board (and also subject to examination by the BOK). In accordance with the agreement reached with ADB concerning auditing of CNB's accounts by an external independent auditor, CNB has appointed San Kyong and Co. to audit its accounts and issue an audit report annually starting with its 1979 accounts. This accounting firm had been accepted by the Bank as auditors of KDB and SMIB. Necessary adjustments will be made by CNB so that its accounting procedures will fully comply with internationally accepted accounting standards in the future.

D. PROSPECTS AND RESOURCE REQUIREMENTS

Operational Projections

4.54 In the aftermath of the devaluation which took place in January 1980, the outlook for the Korean economy is expected to remain favorable and the long-term growth prospects for the manufacturing industries of all sizes are good. GNP is expected to increase in 1979-81 by 9% annually in real terms, with the manufacturing sector growing at an annual rate of 14%. The growth of the economy will continue to be mainly export-led. Export-oriented industries are expected to expand their capacity for production and the

factories which produce for the domestic market are also expected to modernize and expand their facilities and increase their output. Exports of goods and services are projected to increase 17% annually during 1979-81 with manufactured exports providing the bulk of incremental exports. An annual increase in gross fixed investment of around 8% is expected during the Fourth Five Year Plan Period ending 1981. Given the priority assigned to deepening the structure of Korean industries, the small industries are expected to play an increasing role. CNB as an institution assisting small industries has taken that increasing role into account in projecting its operations for the next five years, 1980-84.

4.55 CNB's loan approvals for 1979 reached W 401.5 billion, equally distributed between business loans and general populace loans. This compared with total approvals of W 340.5 billion for 1978 with a similar distribution pattern. Based on the growth trend of its entire loan portfolio during 1976-79, the annual growth rate of loan approvals after 1980 is assumed to be around 30% p.a. with business loans increasing at a slightly faster pace than general populace loans. The projected volume of operations is presented in Annex 21.

4.56 The time lag between approval and commitment and that between commitment and disbursement of local currency loans has been negligible in the past and the pattern is expected to remain unchanged in the future. CNB's foreign currency operations started in the latter part of 1979, and a time lag between different stages has been taken into account in its projections. Around 60% of foreign currency loan approvals are expected to be committed in the current year and 40% in the following year. Around 45% of the commitments are expected to be disbursed in the current year and 55% in the following year.

4.57 CNB expects that the actual overall demand for loans would increase at a higher rate than what it has assumed in making the projections of its own operations. However, strict Government control on credit expansion is expected to continue during the projected period. CNB's lending projections have to be on the conservative side, although CNB's resource mobilization effort is not expected to taper off.

4.58 With respect to small industry's demand for foreign exchange loans, it is estimated to amount to US\$80 million in 1979 (compared with US\$65 million in 1978) and US\$100 million in 1980, based upon various surveys conducted by SMIB and CNB. An estimated increase of 25% per year would not be unrealistic. Therefore, by 1983, the demand would probably reach US\$200 million. CNB, as a new supplier of foreign funds, did not make any foreign currency disbursements in 1979. However, as CNB mobilizes more foreign exchange resources in subsequent years, it expects to contribute around 8% of total demand in 1980 and an average of 17% in 1981-84. This compares with SMIB's estimated average share of 37% during 1979-83. Since no other institutions are equipped to provide long-term foreign currency loans to

small industry, this anticipated resource gap would prompt both CNB and SMIB to raise more foreign currency resources in the next few years.

Resource Requirements

4.59 Local Currency Requirements. CNB's forecast of resource position and requirements for 1980-84 is shown in Annex 22. During the entire projection period, CNB is expected to continue to have surplus short-term resources and to utilize such resources to fill its shortfall in long-term commitments. By 1980, its long-term resource gap would amount to about W 215 billion representing 41% of its long-term loan commitments; the comparative ratios for 1981-84 are 43%, 42%, 41% and 41% respectively. While demand for loans having maturities of more than 5 years is strong, especially as CNB enters into foreign currency loan operations where many firms are likely to need domestic currency funds having maturities over 5 years to match their foreign currency funds, CNB will have to confine itself mainly to making loans with shorter maturities. CNB has received the Government approval to participate in the Small and Medium Industry Promotion Fund; however, this Fund would provide only limited amount of long-term funds. CNB's short-term resource surplus each year during the forecast period is estimated to be more than twice the size of the long-term resource gap, thus enabling CNB to fill such a gap with resources of less than one year's maturity. The remaining portion of the surplus short-term resources would be invested in marketable securities, deposited with those domestic banks that are short of resources, and lent out as call loans.

4.60 Foreign Currency Requirements. Projected foreign currency commitments during the period 1980-84 total about US\$133.1 million (Annex 22). Apart from the loan of US\$10 million which CNB obtained from ADB in the first part of 1979, CNB plans to raise an additional US\$120 million from ADB and IBRD, and US\$3.1 million from the Korean Foreign Exchange Fund during 1980-83. As of December 31, 1984, CNB is expected to have an uncommitted balance of US\$28.5 million. CNB may find it necessary to make a larger contribution in meeting the foreign currency resource demand of the small industry sector by enlarging both its resource mobilization and resource allocation programs in the projection period.

Projected Financial Results

4.61 Projected income statements and projected indicators of financial performance for 1979-84 are shown in Annexes 23 and 25. CNB's low profitability is expected to improve in the next few years. The rate of growth of CNB's gross profit will catch up with the rate of growth of its total assets. However, due to its broad branch network and the costly operations involving numerous transactions with individuals, households and small industrial units, CNB's administrative costs as a percentage of its average total assets would remain high, within the range of 4.1-4.6% during the entire forecast period 1979-84. Profit before provisions and tax for 1979 is estimated at W 4.0 billion, representing an increase of 29% from the level reached in 1978 (W 3.1 billion). It is expected to increase to W 8.7 billion in 1980 and to W 28.3 billion in 1984 representing an average increase of 51% during the six-year projection period. As a percentage of CNB's average total assets, profit before provisions and tax was 0.4% in 1978 and will remain unchanged in 1979. It is expected to go up to 0.7% in 1980 and to 0.9 in 1984. CNB's net profit will not increase in 1979 from the level of W 2.1 billion realized in 1978. It will rise sharply to W 5.9 billion in 1980 and increase to W 19.6 billion by 1984. The expected sharp increase in CNB's profits in 1980 is due to the increase in its paid-in share capital which took place at the end of 1979 and the fact that share capital costs much less to CNB than deposits. CNB's return on average equity, after registering a sharp increase from 5% to 20% in 1975-78, is expected to drop to 8.7% in 1979 because of the increase in share capital mentioned above. The return on average equity will turn upward to 15.1% in 1980, 17.5% in 1981 and 18.4% in 1984. Such returns would not rise sharply because of the expected annual increase in share capital during 1981-84.

Projected Financial Position

4.62 Projected balance sheets for 1979-84 are shown in Annex 24, and selected financial ratios in Annex 25. Based on its operational forecasts, CNB's total assets are expected to increase from W 868.8 billion as of December 31, 1978 to W 1,177 billion as of December 31, 1979 and to W 3,583.8 billion as of the end of 1984, showing an average annual rate of growth of about 27%. Short- and long-term loans are expected to increase from W 434 billion (50% of total assets) in 1978, to W 567.2 billion (48% of total assets) in 1979 to W 988.5 billion (54% of total assets) in 1981 and to W 2,203.5 billion (62% of total assets) in 1984. While the gradual shifting of the asset structure in favor of the loan portfolio is a healthy development, the pace at which this takes place appears to be slow. CNB should take all possible steps to increase its lending operations to match the pace at which the resources are mobilized.

4.63 During the forecast period, the increase of CNB's assets will be financed by additional demand and time deposits which will increase from W 796.1 billion at the end of 1978 to W 3,111.0 billion at the end of 1984, an overall increase of 290%. Total debt will increase from W 849.6 billion in 1978 to W 3,459.8 billion in 1984, while long-term debt will increase from

W 267.6 billion to W 1,143.7 billion over the same period. During the negotiations, the need to increase CNB's share capital to support the rapidly rising debt was discussed. CNB's representatives shared the Bank's view that CNB's equity base needs to be strengthened, and indicated that CNB is prepared to increase its share capital each year during the period 1981-84. While the amount of increase is difficult to estimate precisely, because of the necessity of obtaining the final approval from the National Assembly, CNB will endeavor to increase W 10 billion each year during 1981-84, at the advice of the Bank. Assuming that such capital increases will take place, the projected total debt/equity ratio would drop from the range of 29-33 in 1979-80 to 28-30 in 1981-84. (Without the share capital increases the total debt level would be 42 times equity by 1984). The projected long-term debt/equity ratio, after adjustments, remain below 4:1 during the period from 1979-84, compared to the 7.1 limit agreed upon between ADB and CNB and which is also acceptable to the Bank. The projected current ratio would hover around 1.1:1 during 1979-84, which is within the limit specified by ADB, and also acceptable to the Bank.

4.64 Projected cash flow statements are given in Annex 26. Since the pattern of CNB's resource mobilization and resources allocation is assumed to continue in the future, additional cash surplus is projected each year during 1980-84. The subject of CNB's sizable liquid funds deriving from deposits was reviewed during negotiations. The average maturity of these deposits is very short, in most cases, less than one year. In the present circumstances, bearing in mind the volatile nature of the financial environment in which CNB operates, e.g. the Government's attempt to control inflation by restricting credit, it is regarded generally inappropriate to use the sizable liquid funds deriving from deposits for term lending. However, CNB's management indicated that it would seek ways, in the context of the Government's overall credit policies, to gradually and substantially expand its domestic currency lending operations so as to make fuller use of its existing and prospective deposits, thereby reducing the gap between its resource mobilization and its resource allocation, while at the same time continuing to give due consideration to the nature (generally short-term) of the maturities of these deposits.

5. THE PROPOSED BANK LOAN

Recommendations and Justification

5.01 The continued growth of small-scale industries remains an important element in Korea's development strategy in view of their demonstrated contribution to employment creation, expansion of exports, deepening of the industrial structure, and regional dispersal of industry. The shortage of funds, particularly of term finance available at appropriate terms has been a crucial problem faced by the small enterprises. Statistics available show that the ratio of reliance on bank credit decreases as the size of the enterprises becomes smaller and a considerable number of small enterprises have no alternative but to borrow from the curb market, or to postpone their projects. It is estimated that less than half of the demand for funds from the small enterprises in the past has been satisfied.

5.02 CNB, as the only specialized financial institution catering exclusively to the small industries, is in a position to play a vital role in assisting such firms to meet their financial requirements. CNB has been assisting small industrial firms, including a number of very small ones. During the period from January 1975 to September 1979, 88% of CNB's equipment loans, both by number and by amount, went to projects employing less than 50 workers, including 71% which went to projects employing less than 20 workers. CNB's projects have been highly labor intensive. An analysis of a sample of CNB-financed projects implemented during 1975-78 indicates that the average fixed investment cost-per-job created was around US\$7,885 which is relatively low in Korea. CNB is the only financial institution authorized to handle the Mutual Installment Savings and Remuneration Scheme. This Scheme embodying the principle of linking deposits with lending for specific purposes has proved very effective in attracting deposits and encouraging investments. Because of the assurance of a loan, the small entrepreneur has an inducement to save. Without such assurance, in many cases, there would not be savings enough for investment by SSIs. CNB has an extensive branch network throughout Korea. As of December 31, 1979, CNB had 163 branches while SMIB had 112, KDB 9 and KDFC one. CNB's branches have day-to-day contacts with small industries located in various provinces. Through such a broad network, CNB is in a position to reach out to provide assistance to the SSI sector more effectively.

5.03 In the past, CNB was handicapped by the lack of access to foreign exchange resources as well as long-term domestic funds. On December 19, 1977, CNB's Act was amended to allow CNB to borrow from foreign sources. In May 1979, CNB obtained from ADB a loan of US\$10 million which enabled CNB to start its foreign currency lending operations. In March 1980, CNB was designated as a handling intermediary for the SMI Promotion Fund. Having now obtained access to foreign funds and to the SMI Promotion Fund, CNB is expected to play a larger role in developing and modernizing the small industries in Korea. The Bank has, in the past, been associated with three DFCs in Korea (KDB, KDFC and SMIB). While SMIB has been using the Bank funds to support small- and medium-sized industries, its assistance to the very small ones has been limited and therefore the investment demand of a number of them still remains unsatisfied. CNB, with a branch network which is more extensive than any banking institution in Korea and with a solid clientele built up under the Mutual Installment Savings and Remuneration Scheme, is in a better position to reach the small industries in various regions and help them fill the resource gaps, thus enabling these small enterprises to enhance their contribution to the dispersal of industries, expansion of exports and nonfarm employment creation.

5.04 A Bank loan of US\$30 million is recommended, which is expected to finance approximately 54% of CNB's projected foreign currency loan approvals

/1 CNB is exempted from paying corporate income tax on its income. However, it is required to pay defense tax.

over a two-year period from mid-1980 to mid-1982. The proceeds of the loan will be used primarily to finance procurement of machinery and equipment needed for modernization, rationalization, or expansion of productive capacities of the small enterprises in all regions. It is estimated that the subprojects financed under the proposed loan, approximately 150 in number, would be able to create about 5,000 new jobs. One underlying assumption is that approximately 15-20% of the subprojects would require replacement equipment for rationalization or modernization and the number of new jobs to be created in such cases would be very limited. Starting with this operation, the Bank will be continuously involved in upgrading the project appraisal capabilities within CNB. Given the added function of providing long-term domestic and foreign currency loans, CNB is expected to become more involved in development activities, while maintaining an undiminished role in meeting the short-term financial requirements of the businesses and general populace.

5.05 In sum, the proposed loan will increase the flow of resources to SSI enabling realization of new, modernization and expansion projects, will contribute to greater regional dispersal of investment and will achieve important institution-building objectives by strengthening the capability of CNB to service the needs of the SSI sector in Korea. Particularly at this juncture when Government is making a concerted effort to develop the small- and medium-sized industries (as evidenced by the establishment of a new institution - SMIPC, and granting of new authority to CNB to engage in foreign currency operations), the Bank's association with CNB will assist the Government, CNB and the SSI enterprises in achieving their objectives. The project does not entail any unusual risk.

Main Features of the Loan

5.06 Scope of Financing. The proposed loan will support small industrial, mining and transportation firms with no more than 100 employees and construction and service firms with no more than 20 employees, or firms with total assets not exceeding W 500 million.

5.07 Maximum Size of Subloans. While the current regulations restrict the amount up to which CNB can make term loans in domestic currency to W 30 million (US\$51,724), there is no limitation on its foreign currency loans extended from its foreign resources. In order to ensure that the proceeds of the Bank loan are utilized by a large number of SSI borrowers, it is recommended that the size of individual subloans approved by CNB under the Bank loan will not exceed US\$400,000 equivalent.

5.08 Geographical Distribution of Subloans. To encourage a broader dispersal of the Bank loan outside the metropolitan area, it is recommended that no more than 50% of the loan will be used to finance projects located within the city limits of Seoul.

5.09 Free Limit. In order to enable the Bank to monitor closely the project appraisal work of CNB, an initial free limit of US\$250,000, is proposed. In addition, the first five subprojects to be financed under the loan will be submitted to the Bank for prior approval, irrespective of subloan size. With the proposed free limit it is estimated that roughly one-third of the number of subprojects under this loan (accounting for about one-half of the loan amount) would require prior approval by the Bank.

5.10 Economic Evaluation of Subprojects. In order to ensure that the economic viability of projects will be taken into consideration in the decision-making process, CNB should be encouraged to pay more attention to the economic evaluation of projects. It is recommended that the Economic Rate of Return will be calculated for all subloans above the free limit.

5.11 Component for Financing Smaller Enterprises. Under the current CNB Act and regulations, CNB is permitted to make loans to small-scale manufacturing, mining and transportation enterprises employing 5 to 100 workers and construction and service enterprises employing 5 to 20 workers. In order to ensure access of the smallest firms to Bank funds, it is recommended that at least 50% of the Bank loan be used to make subloans to the SSI firms employing no more than 50 workers or with total assets below W 250 million.

5.12 Debt/Equity Ratio. Under the loan agreement signed between ADB and CNB in May 1979, CNB is required to maintain a long-term debt/equity ratio of 7:1. Debt will include all long-term debt and guarantees but exclude current maturities of such debt, savings under the Mutual Installment Savings and Remuneration Scheme and reserve requirement by Bank of Korea. It is recommended that the same debt/equity ratio be accepted by the Bank.

5.13 Relending Rate. CNB intends to onlend the proceeds of the proposed Bank loan at an interest rate of 2 percentage points above its own borrowing rate (i.e., 10.5% p.a. assuming a Bank relending rate of 8.5% p.a.). This is in line with the general practice of government-owned development financial institutions in Korea in relending the proceeds of their borrowings from institutional sources (IBRD, ADB et al). While during the initial period CNB's costs for processing foreign currency loans may exceed the 2% spread, CNB expects to cover such losses by its earnings on other operations. The interest rate policy on foreign borrowings will be kept under constant review by the Government.

5.14 Financing of Locally Produced Equipment. Sixty percent of the cost of machinery and equipment (including off-the-shelf equipment already imported into the country) procured locally by CNB borrowers, representing the estimated foreign exchange component of such capital goods, will be eligible for financing under the proposed loan.

5.15 Amortization Schedule. As is usual with Bank loans to DFCs, the proposed loan would have a flexible amortization schedule which would substantially reflect the aggregate of the repayment schedules of the individual subloans made by CNB. The loan is expected to be fully repaid within 17 years, including a grace period of 3 years. The estimated disbursement schedule is presented in Annex 28.

Agreements and Understandings Reached at Negotiations

5.16 During loan negotiations:

- (a) understandings were reached with the Government to the effect that:
 - (i) CNB would endeavor to increase its share capital in order to strengthen its equity base as necessary to keep pace with the growth of its liabilities and operations (para. 4.63); and
 - (ii) CNB to be designated in March 1980 as a handling intermediary in allocating the resources made available by SMI Promotion Fund (for which so far only SMIB has been designated as the handling intermediary) (para. 4.19).
- (b) agreements and/or understandings were reached with CNB with respect to:
 - (i) the limitation of the scope of financing under the Bank loan to small industrial, mining and transportation firms with no more than 100 employees and construction and service firms with no more than 20 employees, or firms with total assets not exceeding W 500 million each (para. 5.06);
 - (ii) a ceiling of US\$400,000 on the size of individual subloans (para. 5.07);
 - (iii) a minimum of 50% of the Bank loan for financing subprojects employing up to 50 workers, or with total assets not exceeding W 250 million each (para. 5.11);
 - (iv) a ceiling of up to 50% of the Bank loan for financing subprojects within the city limits of Seoul (para. 5.08);
 - (v) a free limit of US\$250,000, with the first five projects to be submitted to the Bank for prior approval irrespective of size (para. 5.09);
 - (vi) economic rate of return calculation for all subprojects above the free limit (para. 5.10); and

- (vii) the financing of 60% of the cost of machinery and equipment (including off-the-shelf equipment) procured locally by CNB borrowers, representing the estimated foreign exchange component of such capital goods (para. 5.14).

5.17 In addition the Bank reviewed and reached understandings with CNB on the objectives outlined by CNB in its proposed Statement of Development Strategy for 1980/81 (Annex 11).

KOREATHE CITIZENS NATIONAL BANKTrends in the Manufacturing Sector
(Amounts in W billion)

	<u>Number of establishments</u>			<u>No. of workers ('000)</u>			<u>Value added</u>			<u>Investment in tangible fixed assets</u>		
	<u>Sml.</u>	<u>Med.</u>	<u>Lg.</u>	<u>Sml.</u>	<u>Med.</u>	<u>Lg.</u>	<u>Sml.</u>	<u>Med.</u>	<u>Lg.</u>	<u>Sml.</u>	<u>Med.</u>	<u>Lg.</u>
1973	21,392	1,201	700	334	205	618	234	236	911	n.a.	n.a.	n.a.
1974	20,471	1,375	786	345	236	717	307	276	1,284	65	82	442
1975	20,290	1,624	873	371	278	771	430	465	1,932	84	83	671
1976	21,938	1,990	1,029	424	333	961	586	636	2,853	151	145	822
1977	23,299	2,382	1,085	480	403	1,036	886	929	3,782	145	220	971

Source: EPB.

KOREA

CITIZENS NATIONAL BANK

Structure of the Manufacturing Sector, 1977

<u>Sectoral Breakdown</u>	<u>Value added (in W billion)</u>				<u>Employment ('000)</u>			
	<u>Small</u>	<u>/a</u>	<u>Med.</u>	<u>/b</u>	<u>Large</u>	<u>/c</u>	<u>Total</u>	
Food, beverages, tobacco	141.1		186.9		740.7		1,068.7	58.8 29.1 81.4 169.3
Textiles, clothing, leather	179.3		217.7		698.3		1,095.3	138.3 167.7 351.8 657.8
Wood, wood products	43.7		13.9		80.7		138.3	25.0 6.9 38.5 70.4
Paper & paper products	62.7		44.4		125.4		232.5	36.5 17.6 30.5 84.6
Chemicals, rubber, plastics	133.4		160.5		732.8		1,026.7	49.2 37.5 151.7 238.4
Nonmetallic minerals	85.6		70.4		135.7		291.7	24.2 21.1 32.5 77.8
Basic metals	34.3		31.5		260.3		326.1	16.4 13.4 41.2 71.0
Machinery & equipment	179.8		175.5		957.0		1,312.3	109.8 88.2 270.8 468.8
Others	26.2		27.9		51.1		105.2	21.4 22.0 37.6 81.0
<u>Total</u>	<u>886.1</u>		<u>928.7</u>		<u>3,782.0</u>		<u>5,596.8</u>	<u>479.6 403.5 1,036.0 1,919.1</u>
<u>Regional</u>								
<u>Distribution of</u>								
<u>Manufacturing</u>								
Seoul City	272.6		241.8		882.6			145.1 121.5 270.8
Busan City	118.1		126.7		457.8			59.7 61.6 227.7
Gyeonggi Do	170.9		249.4		845.1			82.7 94.5 213.2
Other provinces	324.4		310.7		1,596.5			192.1 125.7 324.3
<u>Total</u>	<u>886.0</u>		<u>928.6</u>		<u>3,782.0</u>			<u>479.6 403.3 1,036.0</u>

/a Small: enterprises employing 5 to 100 workers.

/b Medium: enterprises employing 100 to 300 workers.

/c Large: enterprises employing over 300 workers.

Source: EPB Report on Mining and Manufacturing Survey, 1977.

AEP Projects Department
December 15, 1979

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CITIZEN NATIONAL BANK

Structure of Financial System, 1978

	Assets (W billion)	%	Credit out- standing /a end 1978 (W billion)	No. of branches
A. <u>MONETARY SYSTEM</u>	26,903.6	81.6	-	1,790
1. <u>The Bank of Korea</u>	4,869.4	14.8	-	13
2. <u>Commercial Banking System</u> (Deposit Money Banks)/b	22,034.2	66.8	8,224.6	1,777
a. <u>Commercial Banks</u>	13,626.7	41.3	5,316.9/c	880
(i) Five nationwide commercial banks /d	11,120.9	33.7	3,940.9	550
(ii) Ten local banks	1,524.0	4.6	664.9	286
(iii) Branches of foreign banks	981.8	3.0	711.1	44
b. <u>Specialized Banks</u>	8,407.5	25.5	2,907.7	897
(i) Korea Exchange Bank	4,591.6	13.9	736.3/e	80
(ii) Small-Medium Industry Bank	737.6	2.3	436.6/f	109
(iii) Citizens National Bank	871.0	2.6	446.4/f	162
(iv) Korea Housing Bank	624.4	1.9	378.0/f	90
(v) Credit sector of agri- cultural cooperatives	1,417.0	4.3	785.6/g	367
(vi) Credit sector of fisheries cooperatives	165.9	0.5	124.8/g	89
B. <u>NONBANKING FINANCIAL INSTITUTIONS</u>	6,072.9	18.4	-	2,525
1. <u>Development Banks /h</u>	2,432.9	7.3	1,769.4	23
a. Korea Development Bank	2,029.7/i	6.1	1,451.7/i	17
b. Korea Development Finance Corporation	164.4	0.5	153.3	1
c. Korea Export and Import Bank	238.8	0.7	164.6	5
2. <u>Trust Accounts</u>	868.7	2.6	-	-
3. <u>Insurance Companies</u>	676.4	2.0	-	1,950
a. Life insurance companies	355.0	1.1	-	1,290
b. Nonlife insurance companies	321.4	0.9	-	660
4. <u>Short-Term Finance Companies /j</u>	685.3	2.1	-	11
5. <u>Mutual Savings and Finance Companies /k</u>	215.6	0.7	-	275
6. <u>Postal Savings Accounts</u>	30.1	0.1	-	-
7. <u>Securities Firms</u>	1,163.9	3.6	-	266
a. Korea Securities Finance Corporation	91.8	0.3	-	1
b. Security dealers & brokers (net)	667.3	2.0	-	263
c. Investment trust companies (net)	404.8	1.3	-	2
<u>Total</u>	<u>32,976.5</u>	<u>100.0</u>	<u>-</u>	<u>4,315</u>

/a Calculated only for commercial banking system and the development banks.

/b Deposit money banks as defined by BOK.

/c Comprises loans from banking funds, government funds, foreign loans and personal loans.

/d Excludes trust accounts and accounts of overseas branches, but includes banking account of Bank of Seoul & Trust Company.

/e Comprises loans and discounts, foreign exchange and personal loans.

/f Comprises loans from banking funds, government funds and personal loans.

/g As for /f, but including overdrafts.

/h The Korea Land Bank is excluded.

/i This excludes W 3,898 billion in acceptances.

/j This includes the five merchant banks.

/k Includes credit unions.

Sources: April 1979 Monthly Economic Statistics, BOK; and CNB; and Bank Report 2488-KO.

KOREA

CITIZENS NATIONAL BANK

Rates of Interest in Korea as of January 12, 1980
(Percent per annum)

A. Commercial Banks

<u>Deposit Rates</u>	<u>(%)</u>
a. <u>Time Deposits</u>	
1 month or over (negotiable)	13.14
3 months or over	19.2
6 months or over	21.3
Over 1 year	24.0
b. <u>Installment Savings</u>	
6 months	18.6
1 year	20.6
1-1/2 years	21.6
2 years	22.6
2-1/2 years	23.8
3 years	25.0
c. <u>Wage Earners Savings Scheme /a</u>	
1 year	27.5 (15.4)
2 years	30.3 (16.9)
3 years	33.5 (18.6)
5 years	36.5 (20.6)
d. <u>Demand Deposits</u>	
Temporary deposits	1.0
Passbook deposits	1.8

Lending Rates

a. <u>Operating Funds</u>	
<u>Ordinary Loans</u>	
Prime enterprises	24.5
Other enterprises	25.0

/a Figures in parentheses show the base rates payable by the financial institutions; the remainder is subsidized by Government.

A. Commercial Banks (Cont.)

	<u>(%)</u>
<u>Commercial Notes</u>	
Prime enterprises	24.5
Other enterprises	25.0
<u>Overdraft /a</u>	
Prime enterprises	26.5
Other enterprises	27.0
b. <u>Term Loans /a</u>	
Less than 3 years	24.5
3 to 8 years	25.5
Over 8 years	26.5
c. <u>Export Finance /b</u>	15.0 (12.0)
d. <u>National Investment Fund</u>	22.0
e. <u>Machinery Industry Loans</u>	21.0
f. <u>Loans with Installment Collateral</u>	24.5-25.0
g. <u>Loans on Installment Savings</u>	24.5-25.0
h. <u>Loans Overdue</u>	30.0

/a These rates are 0.5% p.a. higher for the Busan, Daegu, Kyonggi and Kyongnam banks, and 0.5% higher for the other local banks.

/b Rate in parenthesis will be applied until June 30, 1980.

B. Korea Development Bank

	<u>Up to 3</u> <u>years</u> (%)	<u>3 to 8</u> <u>years</u> (%)	<u>Over 8</u> <u>years</u> (%)
<u>Capital Loans /a</u>			
Government Funds	15.0	15.0	15.0
Machine Industry Promotion Funds	21.0	22.0	23.0
Special Equipment Funds	21.0	22.0	-
Internal Funds (priority industries)	21.0	22.0	23.0
Internal Funds (nonpriority industries)	24.5	25.5	26.5
Foreign Commercial Funds /b	18.0	18.0	18.0
<u>Working Capital Loans /a</u>			
Government Funds	15.0	15.0	15.0
Machine Industry Promotion Funds	21.0	21.0	21.0
Special Equipment Funds	21.0	21.0	21.0
Internal Funds (prime clients)	24.5	24.5	24.5
Internal Funds (other clients)	25.0	25.0	25.0
Foreign Commercial Funds /b	18.0	18.0	18.0
<u>National Investment Fund /a /c</u>	21.0	22.0	-
<u>Tourism Development Fund /a /c</u>	25.0	25.0	25.0
<u>Industrial Rationalization Funds /a</u>			
Direct Loans	21.0	22.0	-
Through banking institutions	19.5	20.5	-
<u>Government Special Fund Loans /a /d</u>	7.5-13.5	7.5-13.5	7.5-13.5
<u>Foreign Currency Loans</u>			
Foreign Commercial Funds /e	LIBOR + 1.0	LIBOR + 1.125	LIBOR + 1.25
USAID (3rd loan)	10.0	10.0	10.0
KfW (4th loan)	9.0	9.0	9.0
ADB (5th loan)	9.65	9.65	9.65
IBRD (3rd loan)	9.5	9.5	9.5
<u>Penalty Rate on Overdue Loans</u>	30.0	30.0	30.0

/a In domestic currency.

/b Exchange risk passed on to borrowers.

/c Capital and working capital loans.

/d For power development, shipbuilding, coal mining, public utilities, maritime transportation, railways and roads.

/e Export industries only.

C. Small and Medium Industry Bank

	(%)
<u>Foreign Currency Loans</u>	
IBRD Loan 1175-KO	10.5
IBRD Loan 1507-KO	9.9
IBRD Loan 1749-KO	9.9
ADB fourth loan	10.9
Korea foreign exchange /a	
3 years or less	LIBOR + 1.0
Over 3 years	LIBOR + 1.125
Over 7 years	LIBOR + 1.25

Domestic Currency Loans

Same as commercial banks, KDB

D. Citizens National Bank

Deposit Rates

Checking deposits (business)		-
Temporary deposit		-
Passbook deposits		1.8
Notice deposits (30 days)		10.0
Savings deposits (30 days)		12.6
Time deposit:	3 months	19.2
	6 months	21.3
	1 year	24.0
	Over 1 year	24.0
Installment savings:	6 months	18.6
	12 months	20.6
	18 months	21.6
	24 months	22.6
	30 months	23.8
	36 months	25.0
Property formation savings:	1 year	27.5
	2 years	30.3
	3 years	33.5
	5 years	36.5
Mutual installment receipts	15 months	20.6
	20 months	21.6
	25 months	22.6
	30 months	23.8
	35 months	25.0
	40 months	25.5
	45 months	26.0
	50 months	26.5
	55 months	27.0
	60 months	27.5

/a For ¥ loans, add 1%.

Lending Rates

(%)

Working Capital Loans

On remuneration basis	24.08 - 21.16
On bills	24.5 - 25.0
Overdrafts	26.5 - 27.0
Discount on bills	24.5 - 25.0
On installment savings	24.5 - 25.0

Populace (Consumer) Loans

On remuneration basis	24.08 - 21.16
On bills	25.0
With saving as collateral	25.0
On installment savings	25.0

Facility (Equipment) Loans

On mutual installment basis	24.08 - 21.16
On bills	24.5 - 25.0

E. Bank of Korea

Lending Rates

To: Government	2.0
Exports /a	10.0 (7.0)
Raw material imports	18.0

Discount Rates

Prime enterprises	20.5
Other enterprises	21.0
Other bills	27.0

/a Rate in parenthesis will be applied until June 30, 1980.

KOREA

THE CITIZENS NATIONAL BANK

Major Shareholders
(As of November 30, 1979)

Shareholder	No. of shares	Amount (Won million)	%
Government	6,558,815	3,279.4	65.6
<u>Commercial Banks</u>			
Hanil Bank	792,752	396.4	7.9
Korea First Bank	792,118	396.0	7.9
Cho-Heung Bank	669,872	334.9	6.7
Commercial Bank of Korea	669,872	334.9	6.7
Bank of Seoul and Trust Co.	488,000	244.0	4.9
Others	28,571	14.3	0.3
<u>Total</u>	<u>10,000,000</u>	<u>5,000.0</u>	<u>100.0</u>

AEP Projects Department
December 15, 1979

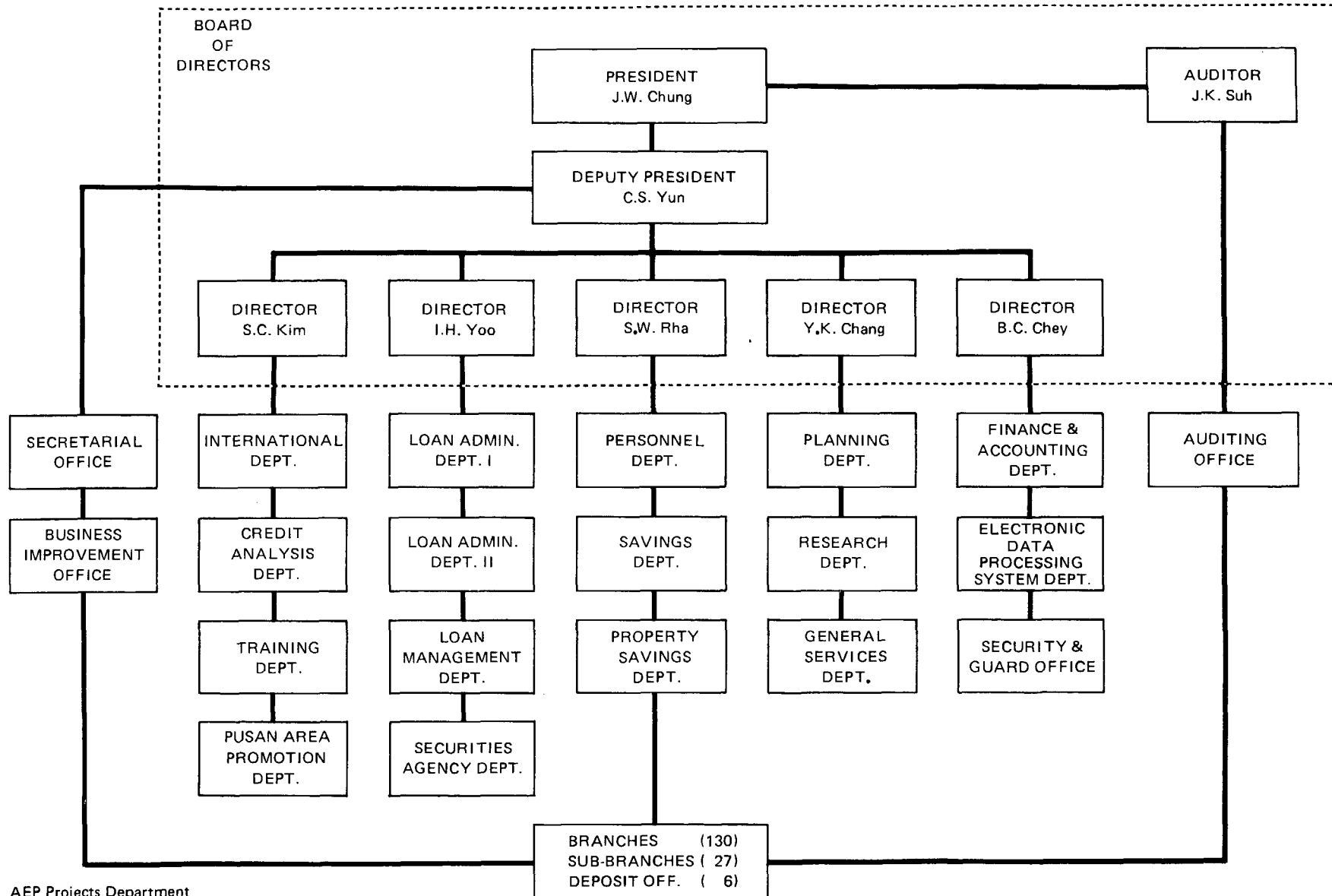
KOREA

THE CITIZENS NATIONAL BANK

Board of Directors
(As of November 30, 1979)

Name	Position	Background
Chung, Jin Wook	President	Career spent mainly in CNB. Joined CNB in 1962. Appointed Director April 1972. Deputy President since February 1976. Appointed President May 1979.
Yun, Chul Soon	Deputy President	Served in BOK from 1948 to 1960, then CNB. Appointed Director June 1973 and Deputy President May 1979.
Kim, Sang Chan	Director	Career spent mainly in CNB. Joined CNB in 1962, Director since June 1975. Reappointed in June 1978.
Yoo, In Ho	Director	Career spent mainly in BOK. Appointed Director in February 1976. Re-appointed February 1979.
Rha, Sung Woong	Director	Career spent mainly in CNB. Joined CNB in 1963. Director since April 1977.
Chey, Byung Churl	Director	Career spent mainly in CNB. Joined CNB in 1963. Director since December 1977.
Chang, Yeung Keun	Director	Served with MOF. Appointed Auditor of CNB in September 1977. Director in May 1979.
Suh, Jai Kyun	Auditor	Career spent mainly in SMIB. Appointed Auditor in May 1979.

KOREA
THE CITIZENS NATIONAL BANK
ORGANIZATION CHART
As of November 30, 1979



KOREA

THE CITIZENS NATIONAL BANK

Staffing as of September 30, 1979

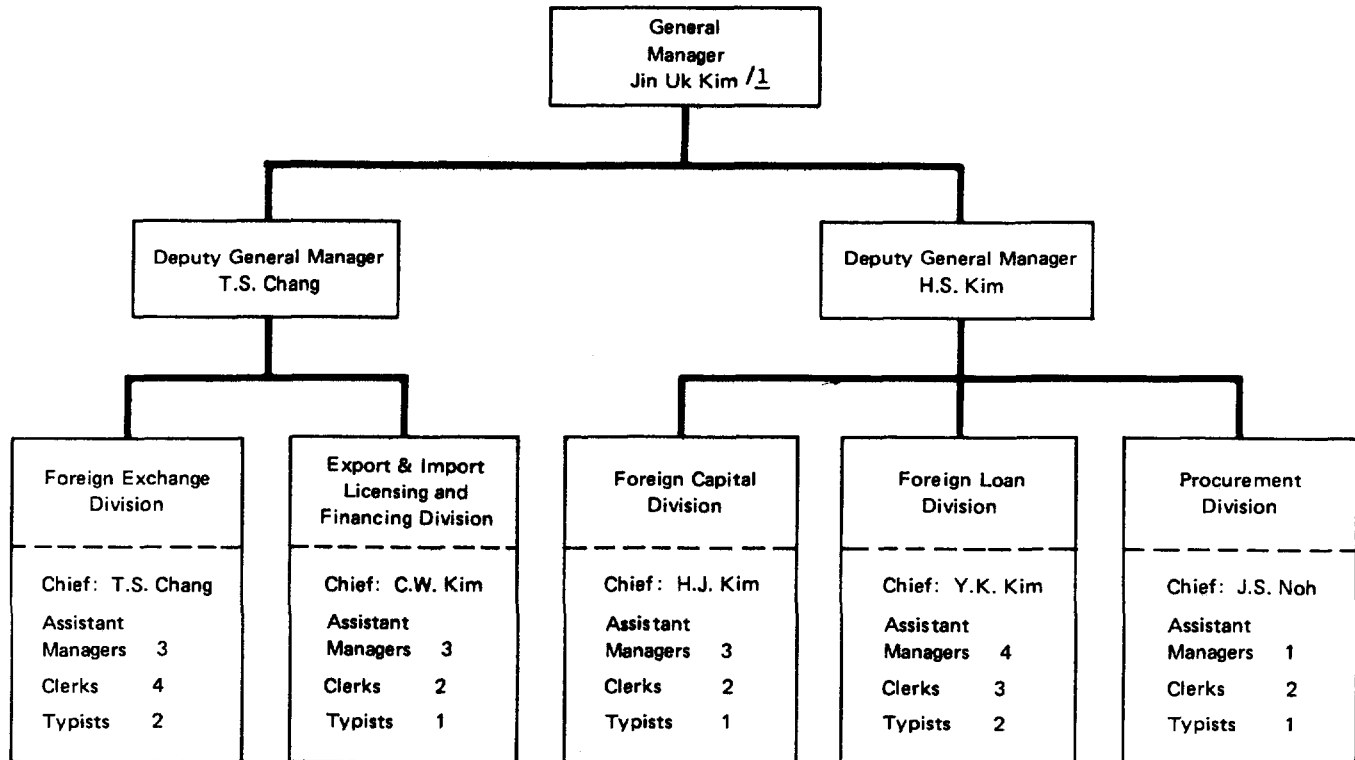
Department	Manager Level						Others			Total
	Financial analyst/accountants	Economist/market analysts	Engineers	Lawyers	Bankers	Sub-total	Clerks	Janitors & others	Sub-total	
International Dept.	5	5	-	5	5	20	22	-	22	42
Planning Dept.	5	2	-	2	4	13	15	-	15	28
Research Dept.	4	4	-	4	2	14	20	3	23	37
Personnel Dept.	5	2	-	4	4	15	25	6	31	46
Educational & Training Department	1	2	-	1	3	7	9	-	9	16
Funds Mgmt. Dept.	5	4	-	5	9	23	58	1	59	82
Savings Dept.	1	3	-	4	3	11	21	2	23	34
Property Formation Savings Dept.	3	1	-	3	2	9	11	-	11	20
Loan Admin. Depts.	2	4	-	5	5	16	19	-	19	35
Credit Analysis Dept.	5	1	4	2	2	14	19	1	20	34
Gen. Svs. Dept.	4	1	2	4	14	25	44	103	147	172
Loan Mgmt. Dept.	1	1	-	2	5	9	9	4	13	22
EDPS Dept.	5	5	-	1	9	20	134	-	134	154
Securities Agency Dept.	1	1	-	3	3	8	32	-	33	41
Security & Guards Office	3	1	-	3	4	11	17	29	46	57
Business Improvement Office	2	1	-	1	2	6	4	-	4	10
Secretarial Office	-	-	-	1	2	3	10	-	10	13
Busan Area Activity Promotion Dept.	2	2	-	1	3	8	5	5	10	18
Auditing Office	9	10	-	11	30	60	5	-	5	65
Subtotal	<u>63</u>	<u>50</u>	<u>6</u>	<u>62</u>	<u>111</u>	<u>292</u>	<u>480</u>	<u>154</u>	<u>634</u>	<u>926</u>
Business Dept. & Branches	235	134	1	139	531	1,040	3,813	637	4,450	5,490
<u>Total</u>	<u>298</u>	<u>184</u>	<u>7</u>	<u>201</u>	<u>642</u>	<u>1,332</u>	<u>4,293</u>	<u>791</u>	<u>5,084</u>	<u>6,416</u>

	<u>Head office</u>	<u>Branches</u>	<u>Total</u>
Professionals	300 /a	1,040	1,340
Non-professionals	634	4,450	5,084
<u>Total</u>	<u>934</u>	<u>5,490</u>	<u>6,424</u>

/a Including 8 members of the Board: President, Deputy President, Directors (5) and Auditor.

AEP Projects Department
December 15, 1979

KOREA
THE CITIZENS NATIONAL BANK
ORGANIZATIONAL STRUCTURE OF THE INTERNATIONAL DEPARTMENT
As of November 30, 1979



Total 41

AEP Projects Department
December 15, 1979

/1 In January 1980, Mr. Kyung Jae Min was appointed General Manager of the International Department to replace Mr. Jin Uk Kim.

World Bank — 21145

KOREA

THE CITIZENS NATIONAL BANK

Policy Statement

(Adopted by the Board of Directors
on August 10, 1979)

Objective

This policy statement is aimed at prescribing CNB's major policy measures related to rendering financial assistance for the promotion of small-scale industry.

Scope of CNB's Operations

CNB shall contribute to the economic development of Korea by promoting, inter alia, the progress and advancement in small-scale industry in conformity with the purposes as stipulated in the CNB Act, its Enforcement Decree and the Government's policies. In order to achieve this objective CNB will expedite the advancement of small-scale enterprises (as defined in the Enforcement Decree of CNB Act and Loan Agreements of the relevant foreign currency borrowings) as follows:

- (a) providing various types of financial assistance such as the lending of mutual installment remunerations (particular type of loan), medium- and long-term facility loans, short-term working capital loans, guarantees, etc; and
- (b) engaging in the activities for the progress of small-scale enterprises such as identification and development of new projects, etc.

Development Policies

CNB will extend its financial assistance to the small-scale enterprises in order to supplement their managerial and financial weakness. Especially preference will be given to the following small-scale enterprises which will effectively contribute to broadening the base of the national economy:

- (a) exporting enterprises designated by the Government;
- (b) import-substitution industries and industries producing raw materials;
- (c) specialized enterprises or industries ancillary to large firms and machinery industries;

- (d) enterprises with potential for export- and import-substitution;
- (e) industries which will develop new products;
- (f) indigenous industries and labor-intensive industries;
- (g) industries effectively contributing to the enhancement of GNP and employment; and
- (h) industries contributing to industrial rationalization and technical development.

General Operating Principles

(a) CNB will carry out its operations in accordance with sound management and business principles and practices. It will expand its operations in the field of small-scale industries.

(b) CNB will finance projects viable from the economic, technical and financial point of view and it will give special attention to the quality of management and the market prospects of projects.

(c) CNB will give assistance to applicants in the course of application for lending and feasibility study.

(d) CNB will determine the repayment period of loans, including grace period depending on nature, individual circumstance of the project and repayment ability of the borrower.

(e) CNB will appropriately supervise the use of its funds, the progress of the project financed and the performance of the enterprise so as to ensure that remedial action is promptly taken when problems arise.

(f) In the case of foreign currency loans, CNB will protect itself against any loss resulting from changes in the rate of exchange between Won and foreign currencies in which CNB's outstanding money obligations will have to be met.

(g) CNB will exert its effort for diversified loan portfolio by industrial sector and geographical allocation, in particular in the execution process of local currency lending except for "Mutual Installment Remuneration." In case of foreign capital subloan, CNB will observe the provisions of the related Loan Agreements.

Financial Guidelines

CNB will endeavor to match maturities of its long-term and short-term loans portfolios with maturities of its resources including deposits.

CNB will not seek to control any of the enterprises in which it has financed nor will it participate in the management of such enterprises except for the purpose of safeguarding its principal and interest.

In accordance with sound banking practices, CNB will secure appropriate collateral for its loans and guarantees. However, in the case of development project loans, CNB will be guided by considerations of technical feasibility, financial viability and economic justification of the projects and enterprises so assisted.

CNB will require eligible borrowers to finance a reasonable portion of the total project cost from their own resources to ensure that they have a reasonable stake in the projects financed by CNB.

Borrowers must not be in arrears in the repayment of either principal and interest on any existing loan.

Limits on Assistance

CNB's total commitments in any one single enterprise in whatever form, i.e., loans, guarantees or a combination thereof, will not exceed 25% of the sum of its unimpaired paid-in capital, reserves and surplus.

CNB's limit on local currency loans and guarantees to any single small-scale industry is the same as stipulated in subparagraphs 1,3 and 3-2, paragraph 1, Article 20 of the Enforcement Decree of the CNB Act. However, with respect to the lending of foreign capital for small-scale industry, CNB is not subject to the above restrictions, but bound by the approval from the Minister of Finance and subject to provisions of Loan Agreements of the relevant foreign currency borrowings.

Management and Organization

CNB will cooperate with its clients in the establishment and implementation of the planned project and will maintain effective organization in order to enhance management capability and intensify training for employees. CNB will also recruit sufficient number of personnel specialized in the field of financial and economic analysis, technique, accounting, law and so on.

Accounting

CNB will maintain adequate accounting records to reflect its business operations and affairs in accordance with generally accepted accounting principles and standards.

CNB will engage a qualified and independent public accountant to audit its books and financial statements every year.

Provisions and Reserves

CNB will annually make appropriate allocations to the account of provision for doubtful loans for the protection against bad debts.

CNB will allocate at least 25% of the profits to a reserve fund every fiscal year until the reserve fund reaches the amount of the paid-in capital.

AEP Projects Department
December 15, 1979

KOREA

THE CITIZENS NATIONAL BANK

Development Strategy for 1980/81 /1

Outline

1. This development strategy is aimed at prescribing major development policy measures of The Citizens National Bank (hereinafter referred to as the CNB) with emphasis given to acceleration of development activities of the CNB for the promotion of small-scale industry.
2. Especially in parallel with the projected expansion of its financing operations in the two-year period 1980/81, CNB shall further expand, apart from its normal financing activity, its developmental and promotional activities particularly in the specific areas outlined below.

Priority Area of Financing

3. CNB shall contribute to the national economic development by expediting the advancement of small-scale enterprise.
4. Thus, main emphasis shall be given to the financial assistance to small-scale enterprises in order to supplement their managerial and financial resources which often lack access to most banking institutions.
5. Especially, the preference in selection of financing beneficiary will be given to the following small-scale enterprises which will effectively contribute to broadening the base of national economy.
 - (a) exporting enterprises designated by the Government;
 - (b) import-substitution industries and industries producing raw materials; and
 - (c) specialized enterprises or industries ancillary to large firms and machinery industries.
 - (d) enterprises with potential for export and import substitution;
 - (e) industries which will develop new products;
 - (f) indigenous industries and labor-intensive industries;

/1 This development strategy will come into effect subject to approval of CNB's Board of Directors.

- (g) industries effectively contributing to the enhancement of GNP and employment; and
- (h) industries contributing to industrial rationalization and technical development.

Project Promotion and Resource Allocation

6. CNB shall make special efforts to assist an increasing number of small-scale enterprises and labor-intensive projects in conformity with the purposes as stipulated in the CNB Act, its Enforcement Decree and the Government's policies.

7. In line with the Government's policy toward geographical distribution of small-scale industry to provincial areas, CNB shall make efforts to increase the proportion of its financing to SSI located in provincial areas by taking advantage of its nationwide branch network.

Resource Mobilization

8. CNB shall endeavor to increase the mobilization of household savings in an effort to augment its domestic currency resources and to introduce sufficient foreign currency resources from international financial institutions. CNB shall also make continued efforts to raise long-term local currency resources from relevant institutions concerned.

Research

9. With a view to providing more diversified financial services, and expanding its operational activities in parallel with the rapidly developing economic environment as well as securing stable basis for mobilization of adequate domestic currency resources, CNB shall strengthen its research capability and activities including "Small Manufacturing Industry Survey," with particular emphasis given on sector studies and market studies for small-scale industry.

Organization

10. In connection with diversification and expansion of its operational activities, CNB shall continue, as a matter of high priority, to enhance professional abilities of its existing staff through adequate training courses provided by domestic and foreign institutions with due consideration given to the fields of financial and economic analysis, appraisal technique, accounting, law, and so on. CNB shall also adopt its organization as appropriate to effectively carry out its expanding activities.

KOREA

THE CITIZENS NATIONAL BANK

Summary of Loan Operations (1975-September 30, 1979)
(Won million)

	1975		1976		1977		1978		Sept. 30, 1979	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
<u>APPROVALS</u> /a										
Working capital loans	43,042	111,984	45,633	108,996	46,412	169,163	34,377	152,463	21,067	136,539
Equipment loans	3,903	7,899	3,884	11,822	4,204	17,332	5,257	17,093	3,879	15,442
<u>Total Business Loans</u>	<u>46,945</u>	<u>119,883</u>	<u>49,517</u>	<u>120,818</u>	<u>50,616</u>	<u>186,495</u>	<u>39,634</u>	<u>169,556</u>	<u>24,946</u>	<u>151,981</u>
General populace loans /b	76,056	67,803	119,499	87,984	153,288	108,488	189,052	170,984	141,732	152,308
<u>Total Approvals</u>	<u>123,001</u>	<u>187,686</u>	<u>169,016</u>	<u>208,802</u>	<u>203,904</u>	<u>294,983</u>	<u>228,686</u>	<u>340,540</u>	<u>166,678</u>	<u>304,289</u>
<u>REPAYMENTS</u>										
Working capital loans	36,386	91,331	31,993	77,630	51,116	138,077	51,947	121,668	26,713	84,223
Equipment loans	1,889	4,533	3,278	7,529	6,359	10,236	4,797	13,546	5,344	11,687
<u>Total Business Loans</u>	<u>38,275</u>	<u>95,864</u>	<u>35,271</u>	<u>85,159</u>	<u>57,475</u>	<u>148,313</u>	<u>56,744</u>	<u>135,214</u>	<u>32,057</u>	<u>95,910</u>
General populace loans /b	73,565	58,852	87,171	62,445	94,065	65,904	143,548	105,191	145,911	119,365
<u>Total Repayments</u>	<u>111,840</u>	<u>154,716</u>	<u>122,442</u>	<u>147,604</u>	<u>151,540</u>	<u>214,217</u>	<u>200,292</u>	<u>240,405</u>	<u>177,968</u>	<u>215,275</u>
<u>OUTSTANDING</u>										
Working capital loans	63,733	112,182	77,373	143,548	72,669	174,634	55,099	205,429	49,453	257,745
Equipment loans	9,695	17,349	10,301	21,642	8,146	28,738	8,606	32,285	7,141	36,040
<u>Total Business Loans</u>	<u>73,428</u>	<u>129,531</u>	<u>87,674</u>	<u>165,190</u>	<u>80,815</u>	<u>203,372</u>	<u>63,705</u>	<u>237,714</u>	<u>56,594</u>	<u>293,785</u>
General populace loans /b	95,049	62,345	127,377	87,884	186,600	130,468	232,104	196,261	227,925	229,204
<u>Total Outstanding</u>	<u>168,477</u>	<u>191,876</u>	<u>215,051</u>	<u>253,074</u>	<u>267,415</u>	<u>333,840</u>	<u>295,809</u>	<u>433,975</u>	<u>284,519</u>	<u>522,989</u>

/a Given the nature of domestic currency operations, approvals are simultaneous with commitments and disbursements.

/b Including households and individuals.

AEP Projects Department
December 15, 1979

KOREA

THE CITIZENS NATIONAL BANK

Characteristics of Equipment Loans Approved (1975-September 30, 1979) /a
(Won million)

	1975			1976			1977			1978			September 30, 1979		
	No.	Amount	%	No.	Amount	%	No.	Amount	%	No.	Amount	%	No.	Amount	%
A. Sectoral Distribution															
Manufacturing															
Food, beverage and tobacco	253	320	4.0	245	528	4.5	273	734	4.2	292	802	4.7	105	410	2.7
Textile, wearing apparel & leather	571	1,485	18.8	568	2,205	18.7	616	3,239	18.7	831	3,656	21.4	456	2,264	14.7
Wood and wood products	39	747	9.4	36	1,172	9.9	31	1,716	9.9	45	1,746	10.2	39	573	3.7
Paper, paper products and printing	41	512	6.5	347	788	6.7	382	1,155	6.7	427	1,115	6.5	173	705	5.6
Chemicals, petroleum, coal, rubber and plastic	560	932	11.8	419	1,096	9.2	439	1,606	9.3	493	1,762	10.3	224	808	5.2
Nonmetallic mineral products	194	406	5.1	199	586	4.9	216	858	4.9	403	692	4.1	123	305	2.0
Basic metals	232	292	3.7	234	404	3.4	249	593	3.4	292	720	4.2	79	215	1.4
Metal products, machinery and equipment	773	745	9.4	555	1,298	11.0	601	1,981	11.5	789	1,973	11.5	446	1,183	7.7
Others	-	-	-	-	-	-	-	-	-	-	-	-	180	1,002	8.3
Total Manufacturing	2,663	5,439	68.7	2,603	8,077	68.3	2,807	11,882	68.6	3,572	12,466	72.9	1,825	7,465	48.4
Mining	18	95	1.2	25	142	1.2	30	243	1.4	34	279	1.6	12	87	0.5
Transportation	358	692	8.8	363	1,039	8.8	390	1,489	8.6	491	1,387	8.1	1,039	4,203	27.2
Construction	142	371	4.7	141	551	4.7	152	801	4.6	209	795	4.7	92	473	3.1
Others	722	1,302	16.6	752	2,013	17.0	825	2,917	16.8	951	2,166	12.7	911	3,214	20.8
Total	3,903	7,899	100.0	3,884	11,822	100.0	4,204	17,332	100.0	5,257	17,093	100.0	3,879	15,442	100.0
B. Geographical Distribution															
Seoul city	2,384	4,423	56.0	2,328	6,608	55.9	2,518	9,939	57.3	3,163	9,727	56.9	2,024	7,169	46.4
Kyong-gi province	147	300	3.8	144	638	5.4	160	884	5.1	189	929	5.4	207	934	6.0
South Chungchung province	211	419	5.3	214	413	3.5	227	555	3.2	283	581	3.4	163	671	4.3
North Chungchung province	93	189	2.4	95	213	1.8	101	276	1.6	116	301	1.8	64	317	2.0
Kang Won province	82	166	2.1	82	556	4.7	91	797	4.6	107	807	4.7	79	415	2.7
South Jeon Ra province	95	250	3.2	128	409	3.4	147	607	3.5	163	612	3.6	135	551	3.6
North Jeon Ra province	121	244	3.1	120	354	3.1	130	526	3.1	158	524	3.1	163	523	3.4
South Kyungsang province	194	394	5.0	194	551	4.7	210	814	4.7	294	821	4.8	210	860	5.6
North Kyungsang province	261	521	6.5	263	907	7.6	280	1,335	7.7	364	1,345	7.9	292	1,464	9.5
Busan city	285	930	11.8	284	1,078	9.1	307	1,461	8.4	373	1,307	7.6	512	2,420	15.7
Cheju province	30	63	0.8	32	95	0.8	33	138	0.8	47	139	0.8	30	118	0.8
Total	3,903	7,899	100.0	3,884	11,822	100.0	4,204	17,332	100.0	5,257	17,093	100.0	3,879	15,442	100.0
C. Size of Loans															
Up to W 1 million	589	300	3.8	586	460	3.9	630	410	2.4	617	366	2.2	331	149	0.9
W 1 mil. to W 5 mil.	2,886	4,172	52.8	2,870	8,060	68.2	3,007	11,050	63.7	3,559	6,236	36.5	2,758	7,410	48.0
W 5 mil. to W 10 mil.	390	2,897	36.7	388	2,522	21.3	420	2,940	17.0	744	4,672	27.3	536	3,998	25.9
W 10 mil. to W 20 mil.	38	530	6.7	40	780	6.6	103	1,751	10.1	229	3,146	18.4	189	2,310	15.0
W 20 mil. to W 30 mil.	-	-	-	-	-	-	44	1,181	6.8	108	2,673	15.6	65	1,575	10.2
Total	3,903	7,899	100.0	3,884	11,822	100.0	4,204	17,332	100.0	5,257	17,093	100.0	3,879	15,442	100.0
D. Number of Workers															
5 to 20 workers	3,434	6,564	83.1	3,281	9,469	80.0	3,161	12,132	70.0	3,037	12,115	70.9	2,275	9,012	58.5
20 to 50 workers	317	762	9.6	338	1,641	13.9	494	3,334	19.2	1,197	2,094	12.2	1,137	4,506	29.2
50 to 100 workers	37	236	2.9	152	358	3.0	423	1,029	5.9	764	1,717	10.0	379	1,503	9.8
Subtotal	(3,788)	(7,562)	(95.6)	(3,771)	(11,468)	(96.9)	(4,078)	(16,495)	(95.1)	(4,998)	(15,926)	(93.1)	(3,791)	(15,021)	(97.5)
More than 100 workers	115	337	4.4	113	354	3.1	126	837	4.9	259	1,167	6.9	88	421	2.5
Total	3,903	7,899	100.0	3,884	11,822	100.0	4,204	17,332	100.0	5,257	17,093	100.0	3,879	15,442	100.0
E. Duration of Loans															
Up to 1 year	54	239	3.0	47	609	5.1	43	516	3.0	39	407	2.4	4	48	0.3
1 to 3 years	2,071	4,264	54.0	1,836	6,265	53.0	2,312	9,520	54.9	2,657	10,207	59.7	2,657	10,761	69.7
3 to 5 years	1,778	3,396	43.0	2,001	4,948	41.9	1,849	7,296	42.1	2,561	6,479	37.9	1,218	4,633	30.0
Total	3,903	7,899	100.0	3,884	11,822	100.0	4,204	17,332	100.0	5,257	17,093	100.0	3,879	15,442	100.0

/a This table covers all equipment loans, including those on mutual remuneration and appraisal basis.

KOREA

THE CITIZENS NATIONAL BANK

Socioeconomic Impact of a Sample of Equipment Loan from 1975 to 1978 /a

	1978
No. of projects	87
Total project cost (Won million)	4,423
CNB's financing (Won million)	1,557
Share of CNB's financing (%)	35.2
Incremental annual sales (Won million)	7,300
Incremental annual value added (Won million)	2,745
No. of direct additional employment	806
of which: skilled	247
unskilled	422
others	137
Incremental annual gross exports (US\$ million)	1.6
Increase in fixed assets (Won million)	3,082
<u>Memorandum Items</u>	
Sales per employee (Won '000)	9,057
Value added per employee (Won '000)	3,406
Investment per employee (Won '000)	3,824
Ratio of sales to fixed assets (incremental)	2.4
Ratio of value added to fixed assets (incremental)	0.9
Ratio of value added to sales (incremental)	0.4
Export share of sales (%)	10.6

/a Table based on a very limited sample of 87 small industry equipment loans of more than W 10 million made before July 1977.

AEP Projects Department
December 15, 1979

KOREA

THE CITIZENS NATIONAL BANK

Equity Portfolio as of September 30, 1979
(Won thousand)

Name of Company	Amount at cost	No. of shares	% of total shares	Dividends (1978)	Financial situation (profitable or not profitable)
<u>Korea Housing Bank</u>	200,000	400,000	1.07	4,000	profitable
<u>Bukook Mutual Savings and Finance Company</u>	1,499,770	1,499,700	99.99	0	not profitable
<u>Korea General Chemical Corp.</u>	327,887	655,773	0.37	0	not profitable
<u>Others</u>	<u>25,720</u>	<u>34,216</u>	-	<u>3,130</u>	-
Dae Han Electric Co., Ltd.	10,193	12,690	0.03	704	profitable
Mi Won Industrial Co., Ltd.	1,381	1,735	0.02	217	profitable
Seoul Mi Won Industrial Co. Ltd.	8,172.	11,104	0.11	1,338	"
Dae Han Ink & Painting Co. Ltd.	2,584	3,201	0.06	329	"
Yoo Han Pharmacy Co., Ltd.	936	857	0.01	28	"
Peyng Ann Textile Co., Ltd.	672	1,399	0.08	175	"
Sam Jin Aluminum Co., Ltd.	228	380	0.03	48	"
Sam Sung Paper Manufacturing Co., Ltd.	271	615	0.05	62	"
Sam Sung Pharmacy Co., Ltd.	396	966	0.05	0	not profitable
Dong Kook Heavy Machinery Co., Ltd.	757	1,009	0.06	202	profitable
Il Shin Steel Co., Ltd.	130	260	0.002	27	"
<u>Total</u>	<u>2,053,377</u>			<u>7,130</u>	

AEP Projects Department
December 15, 1979

KOREA

THE CITIZENS NATIONAL BANK

Summarized Balance Sheets (1975-September 30, 1979)
(Won million)

As of December 31,	1975	1976	1977	1978	Sept. 30 1979
<u>ASSETS</u>					
<u>Current Assets</u>					
Cash and checks	9,304	13,485	27,532	63,976	104,817
Due from Bank of Korea /a	34,410	45,802	69,379	79,646	128,037
Deposits with other domestic banks	8,798	18,515	99,294	60,007	97,341
Foreign currency deposits	-	6	20	29	56
Short-term loans:					
Business loans	4,434	5,526	5,817	4,690	46,453
General populace loans /b	2,129	2,724	4,698	23,016	32,965
<u>Total Short-Term Loans</u>	<u>6,563</u>	<u>8,250</u>	<u>10,515</u>	<u>27,706</u>	<u>79,418</u>
Securities	320	14,066	1,361	19,246	79,015
Call loans	-	-	-	90,000	50,000
Current maturities					
Securities and deposits	6,485	12,480	43,021	93,729	93,188
Term loans	110,217	145,752	140,081	251,804	266,809
Other current assets	1,986	2,497	2,911	5,966	3,994
<u>Total Current Assets</u>	<u>178,083</u>	<u>260,853</u>	<u>394,114</u>	<u>692,109</u>	<u>902,675</u>
<u>Medium/Long-Term Assets</u>					
Medium-term deposits with domestic banks	879	673	435	239	102
Term loans:					
Business loans	50,991	66,712	114,071	85,167	109,125
General populace loans /b	24,105	32,360	69,173	69,298	67,637
<u>Total Term Loans</u>	<u>75,096</u>	<u>99,072</u>	<u>183,244</u>	<u>154,465</u>	<u>176,762</u>
Less: Provisions for doubtful loans	(1,031)	(1,017)	(1,190)	(924)	(1,715)
<u>Net Term Loan Portfolio</u>	<u>74,065</u>	<u>98,055</u>	<u>182,054</u>	<u>153,541</u>	<u>175,047</u>
Equity investments	1,868	1,871	2,049	2,752	2,053
Other medium/long-term assets	2,193	2,656	4,177	9,848	12,765
<u>Fixed Assets</u>					
Premises & equipment (net)	6,498	7,465	8,195	10,303	20,737
<u>Deferred Accounts</u>					
	-	-	-	-	17
<u>Total Assets</u>	<u>263,586</u>	<u>371,573</u>	<u>591,024</u>	<u>868,792</u>	<u>1,113,396</u>

/a Including BOK's reserve requirements.

/b Including households and individuals.

As of December 31,	1975	1976	1977	1978	Sept. 30 1979
LIABILITIES AND EQUITY					
Current Liabilities					
Demand deposits	59,696	83,193	111,641	161,173	222,724
Time and savings deposits	76,035	101,154	190,364	291,867	395,820
Subtotal	<u>135,731</u>	<u>184,347</u>	<u>302,005</u>	<u>453,040</u>	<u>618,544</u>
Short-term borrowings	-	21	1,690	-	-
Debentures issued	-	-	-	-	1,516
Current maturities					
Deposits	26,611	41,642	42,385	78,240	145,520
Borrowings	27	7	-	-	-
Other current liabilities	12,157	17,926	30,658	50,699	57,961
Total Current Liabilities	<u>174,526</u>	<u>243,943</u>	<u>376,738</u>	<u>581,979</u>	<u>823,541</u>
Medium/Long-Term Liabilities					
Mutual installment receipts	59,345	75,216	97,802	121,314	129,753
Time & savings deposits	17,693	24,834	41,979	60,683	38,556
Property formation savings deposits	-	15,296	60,194	82,779	78,352
Total Term Deposits	<u>77,038</u>	<u>115,346</u>	<u>199,975</u>	<u>264,776</u>	<u>246,661</u>
Borrowings:					
BOK	1,500	1,500	1,500	1,500	1,779
KDB	-	30	30	27	5
Government	1,600	1,450	1,300	1,000	623
Debentures issued	879	673	435	239	134
Other long-term liabilities	19	13	16	35	24
Total Medium/Long-Term Liabilities	<u>81,036</u>	<u>119,012</u>	<u>203,256</u>	<u>267,577</u>	<u>249,226</u>
Provisions for Retirement Grants					
	384	384	1,660	8,160	13,718
Equity					
Paid-in capital	4,500	4,500	5,000	5,000	5,000
Capital surplus	10	10	10	10	13,871/a
Legal reserves	745	841	1,095	1,395	1,922
Other reserves	2,275	2,275	2,575	2,925	4,124
Retained earnings	110	608	690	1,746	20
Current year's profit (loss)	-	-	-	-	1,974
Total Equity	<u>7,640</u>	<u>8,234</u>	<u>9,370</u>	<u>11,076</u>	<u>26,911</u>
Total Liabilities and Equity	<u>263,586</u>	<u>371,573</u>	<u>591,024</u>	<u>868,792</u>	<u>1,113,396</u>
RATIOS					
Current ratio	1.02:1	1.07:1	1.05:1	1.19:1	1.09:1
Current ratio (adjusted) /b	1.02:1	1.08:1	1.05:1	1.20:1	1.10:1
Total debt/equity	33.50:1	44.13:1	62.07:1	77.40:1	40.37:1
Long-term debt/equity	10.61:1	14.46:1	21.69:1	24.17:1	9.26:1
(adjusted) /c	4.00:1	6.20:1	12.40:1	14.40:1	5.25:1
Reserves & provisions as % of loan portfolio	2.17	1.87	1.61	1.60	4.52

/a Including W 13,861 million of assets revaluation; W 13,800 million of which would be reclassified as paid-in-capital at the year end.

/b Current assets + current maturities - remunerated mutual installment savings to current liabilities + current maturities - remunerated mutual installment savings.

/c Long-term debt + long-term guarantees - current maturities - reserve requirements by Bank of Korea - remunerated mutual installment savings to total unimpaired paid-in-capital, surplus and reserves.

KOREA

THE CITIZENS NATIONAL BANK

Summarized Income Statements (1975-September 30, 1979)
(Won million)

	1975	1976	1977	1978	Sept. 30 1979
<u>INCOME</u>					
Interest on business loans	17,553	21,432	28,460	35,133	33,704
Interest on general populace loans	8,260	10,555	16,520	26,062	26,293
Interest on deposits with domestic banks	1,486	1,776	11,306	16,625	15,796
Interests on securities	920	1,965	2,980	12,531	22,429
<u>Total Interest Income</u>	<u>28,219</u>	<u>35,728</u>	<u>59,266</u>	<u>90,351</u>	<u>98,222</u>
Dividends on investments	34	12	192	6	7
Profit on sales of securities & investments	127	-	25	137	250
Fees and commissions	586	775	1,033	1,366	1,025
Other income	3,080	2,404	2,907	6,846	9,754
<u>Gross Income</u>	<u>32,046</u>	<u>38,919</u>	<u>63,423</u>	<u>98,706</u>	<u>109,258</u>
<u>EXPENSES</u>					
Interest on mutual installment receipts	6,217	7,660	11,033	14,059	13,761
Interest on deposits	12,514	16,084	31,149	48,874	58,609
Interest on borrowings	263	222	189	161	127
<u>Total Interest Expenses</u>	<u>18,994</u>	<u>23,966</u>	<u>42,371</u>	<u>63,094</u>	<u>72,497</u>
Fees and commissions	199	284	442	433	120
Contribution to Credit Guarantee Fund	798	994	1,143	1,044	888
General administrative expenses	11,083	12,083	17,524	27,070	29,490
Other expenses	246	218	319	3,961	2,971
<u>Total Expenses</u>	<u>31,320</u>	<u>37,545</u>	<u>61,799</u>	<u>95,602</u>	<u>105,966</u>
<u>Income Before Provisions and Tax</u>	<u>726</u>	<u>1,374</u>	<u>1,624</u>	<u>3,104</u>	<u>3,292</u>
Provisions for doubtful loans	-	-	192	734	800

	1975	1976	1977	1978	Sept. 30 1979
<u>Income Before Tax</u>	<u>726</u>	<u>1,374</u>	<u>1,432</u>	<u>2,370</u>	<u>2,492</u>
Tax	337	466	418	264	218
<u>Net Income</u>	<u>389</u>	<u>908</u>	<u>1,014</u>	<u>2,106</u>	<u>2,274</u>
<u>Appropriations</u>					
Dividends	305	314	378	400	-
Reserves	96	554	650	1,726	-
Unappropriated retained earnings	(12)	40	(14)	(20)	-
<u>Total</u>	<u>389</u>	<u>908</u>	<u>1,014</u>	<u>2,106</u>	<u>-</u>
<u>RATIOS</u>					
<u>As Percentage of Average</u>					
<u>Total Assets</u>					
Gross income	13.2	12.3	13.2	13.5	11.0
Financial expenses	7.9	7.6	8.9	8.6	7.3
Gross spread (Gross income - financial expenses)	5.3	4.7	4.3	4.9	3.7
Return	8.1	8.0	9.1	9.0	7.6
General administrative expenses	4.6	3.8	3.6	3.7	3.0
Provisions	0.4	0.3	0.3	0.1	0.1
Income before provisions and tax	0.3	0.4	0.3	0.4	0.3
Net income	0.2	0.3	0.2	0.3	0.2
<u>Other Ratios</u>					
Net income as % of average equity	5.1	11.4	11.5	20.6	12.0
Income on business loans as % of average business loans outstanding	13.6	14.5	15.4	15.9	12.7
Income on populace loans as % of average populace loans outstanding	13.2	14.1	15.1	16.0	12.4
Cost of deposits as % of average deposits outstanding	7.8	8.2	9.5	9.4	8.0
Cost of debt as % of average debt outstanding	6.5	5.8	5.5	5.3	4.8
Dividend rate (%)	7	7	8	8	-
Dividend payout	78	35	37	18.9	-
Book value as % of par	170	183	187	222	-
Interest cover	3.98	4.06	4.01	3.88	-
Debt service cover	1.55	1.88	1.79	1.82	-

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THE CITIZENS NATIONAL BANK

Summarized Cash Flow Statement (1975-September 30, 1979)
(Won million)

	1975	1976	1977	1978	Sept. 30 1979
I. Sources					
Operations:					
Net income	389	908	1,014	2,106	2,274
Non-cash charges /a	729	332	2,645	8,740	8,100
Less:					
Non-cash profit /b	-	-	-	983	-
Subtotal	<u>1,118</u>	<u>1,240</u>	<u>3,659</u>	<u>9,863</u>	<u>10,374</u>
Received in mutual					
installment receipts	71,901	93,904	129,590	161,458	140,851
Received in deposits	2,852,303	3,890,291	7,100,107	12,502,659	14,119,742
Borrowings: Bank of Korea	22,720	365	35	-	279
Others	23,440	2,150	16,750	153,390	12,170
Issued Property Formation					
Debentures	-	-	-	-	1,548
Increase in other liabilities	90,353	138,578	224,494	282,881	439,808
Increase in Paid-in capital	-	-	500	-	-
Subtotal	<u>3,060,717</u>	<u>4,125,288</u>	<u>7,471,476</u>	<u>13,100,388</u>	<u>14,703,895</u>
Collections:					
Loans for business	98,198	85,159	148,313	135,197	95,910
Loans for general populace	56,503	62,431	65,886	105,191	119,356
Call-loan	164,640	470,410	684,040	1,481,900	2,898,800
Withdrawn in deposits with					
domestic banks	458,224	833,809	1,383,147	3,804,704	3,874,912
Sale of securities	17,143	25,388	47,758	236,769	90,044
Sale of premises and equipments	434	464	255	1,539	357
Decrease in other assets	3,956	4,846	4,996	9,916	11,239
Subtotal	<u>799,098</u>	<u>1,482,507</u>	<u>2,334,395</u>	<u>5,775,216</u>	<u>7,090,618</u>
Total Sources	<u>3,860,933</u>	<u>5,609,035</u>	<u>9,809,530</u>	<u>18,885,467</u>	<u>21,804,887</u>
II. Uses					
Disbursements:					
Loans for business	119,883	120,818	186,495	169,556	151,981
Loans for general populace	67,803	87,984	108,488	170,984	152,308
Call-loan	164,640	470,410	684,040	1,571,900	2,858,800
Deposited with domestic banks	463,509	861,096	1,502,902	3,796,147	3,950,627
Purchase of securities	20,462	38,748	50,135	285,406	158,446
Acquired new premises and					
equipments	1,396	1,763	1,334	3,996	2,208
Increase in other assets	3,979	5,819	7,159	18,636	12,201
Subtotal	<u>841,672</u>	<u>1,586,638</u>	<u>2,540,533</u>	<u>6,016,625</u>	<u>7,286,571</u>
Withdrawn in mutual install-					
ment receipts	53,285	72,514	101,587	131,299	112,174
Withdrawn in deposits	2,832,310	3,809,726	6,925,080	12,281,127	13,923,427
Repaid against borrowings	44,889	2,820	15,504	499	12,706
Decrease in other liabilities	87,273	132,845	211,742	418,135	428,079
Subtotal	<u>3,017,757</u>	<u>4,017,905</u>	<u>7,253,913</u>	<u>12,831,060</u>	<u>14,476,206</u>
Paid dividends	250	305	314	378	400
Paid retirement grants /c	324	-	689	951	842
Subtotal	<u>574</u>	<u>305</u>	<u>1,003</u>	<u>1,329</u>	<u>1,242</u>
Total Uses	<u>3,860,003</u>	<u>5,604,848</u>	<u>9,795,469</u>	<u>18,849,014</u>	<u>21,764,019</u>

/a Including costs of depreciation on tangible fixed assets, provisions on doubtful loans, and provisions for retirement grants.

/b Including transfer of remaining amount of provisions on doubtful loans.

/c Retirement Grants for 1976 were paid in General Administrative Expenses, so figure in "Paid Retirement Grants" of the year is not shown.

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THE CITIZENS NATIONAL BANK

Analysis of Loan Portfolio in Arrears, 1975-79
(Won million)

As of December 31,	1975		1976		1977		1978		Sept. 30, 1979	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
A. Portfolio Status										
Total loans outstanding	168,477	191,876	215,051	253,074	267,415	333,840	295,809	433,975	284,519	522,989
Less: Outstanding loans in grace period	-	-	-	-	295	3,960	358	4,416	295	4,334
Loans in repayment stage	168,477	191,876	215,051	253,074	267,120	329,880	295,451	429,559	284,224	518,655
Outstanding amount of loans affected by arrears	32,322	39,111	29,286	33,855	31,485	38,542	31,502	41,648	41,895	4,481
Arrears										
Principal	32,322	2,768	29,286	2,170	31,485	2,293	31,502	2,447	41,895	4,481
Interest		1,245		873		1,062		2,119		/a
Total Arrears		<u>4,013</u>		<u>3,043</u>		<u>3,355</u>		<u>4,566</u>		
Loans affected by arrears as % of total loans outstanding	19.2%	20.4%	13.6%	13.4%	11.8%	11.5%	10.7%	9.6%	14.7%	17.0%
Total arrears as % of total loans outstanding		2.1%		1.2%		1.0%		1.1%		0.9%/a
Total arrears of principal as % of total loans in repayment stage		1.4%		0.9%		0.7%		0.6%		0.9%
Collection rate (%)										
Principal		97.8		98.4		98.7		99.0		98.0
Interest		95.4		97.4		97.7		96.7		
Total		97.4		98.2		98.4		98.5		
B. Reschedulings and Write-offs										
Loans rescheduled	2,383	3,903	1,985	3,302	3,226	6,448	5,147	16,228	3,119	17,878
Loans written off	23	15	104	14	702	18	21	17	14	9
C. Aging of Loan Arrears as of September 30, 1979										
	<u>Number</u>		<u>Outstanding loans affected by arrears</u>		<u>Total principal arrears</u>					
1 - 3 months	38,014		81,191		3,485					
3 - 6 months	3,441		6,912		782					
6 - 12 months	375		439		109					
12 - 24 months	65		219		105					
Over 24 months	-		-		-					
	<u>41,895</u>		<u>88,761</u>		<u>4,481</u>					
D. Loan Amounts Consigned to the Korea Readjustment Corporation for Collection /b										
Consigned	-	-	-	-	3	26	8	105	4	48
Collected	-	-	-	-	2	13	2	48	8	94

/a Interest arrears as of September 30, 1979 are not available.

/b These amounts are included in arrears shown above.

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THE CITIZENS NATIONAL BANK

Resource Position as of December 31, 1979

		<u>Amount</u>
I. <u>Domestic Currency</u> (Won million)		
A. <u>Long-Term Resources</u>		
Equity: Paid-in capital	30,000	
Reserves and retained earnings	8,260	
<u>Total Equity</u>		<u>38,260</u>
Borrowings: Government	423	
BOK	279	
KDB	4	
Property formation debentures	35	
Savings deposits (over one year)	402,191	
<u>Total Borrowings</u>		<u>402,932</u>
<u>Total Long-Term Domestic Currency Resources</u>		<u>441,192</u>
Less: Term loans outstanding	470,956	
Fixed assets (net)	26,361	
Investment in securities	61,947	
BOK's reserve requirement	15,680	
Other long-term assets	15,598	
<u>Total Long-Term Lending and Investments</u>		<u>590,542</u>
<u>Long-Term Resources Available for Further Commitment and Disbursement /a</u>		<u>(149,350)</u>
B. <u>Short-Term Resources</u>		
Demand and savings deposits (less than 1 year)	648,526	
Property formation debentures	1,818	
<u>Total Short-Term Domestic Currency Resources</u>		<u>650,444</u>
Less: Short-term loans outstanding	96,282	
Investment in securities	-	
Other current assets	-	
BOK's reserve requirement	143,892	
<u>Total Short-Term Lending and Investments</u>		<u>240,174</u>
<u>Short-Term Resources Available for Further Commitment and Disbursement /a</u>		<u>410,270</u>
C. <u>Total Domestic Currency Resources</u>		
Total Long-Term resources	441,192	
Total Short-Term resources	650,444	
<u>Total Domestic Currency Resources</u>		<u>1,091,636</u>
Less: Total Long-Term lending & investments	590,542	
Total Short-Term lending & investments	240,174	
<u>Total Domestic Currency Lending and Investments</u>		<u>830,716</u>
<u>Total Domestic Currency Resources Available for Further Commitment and Disbursement /a</u>		<u>260,920</u>
II. <u>Foreign Currency Resources</u> (US\$ million)		
Long-Term borrowings from ADB	5,829	
Less: Foreign currency loans disbursed	0	
Resources available for further disbursement	5,829	
Less: Undisbursed loan commitments	584	
Resources available for further commitments	5,245	
Less: Uncommitted approvals	438	
<u>Net Resources Available for Further Approvals</u>		<u>4,807</u>

/a Assuming that the time lag between commitment and disbursement is negligible.

AEP Projects Department
February 29, 1980

KOREA

THE CITIZENS NATIONAL BANK

Projected Operations, 1979-84 /a
(Won million)

	1979	1980	1981	1982	1983	1984
<u>Approvals</u>						
<u>Business Loans /b</u>						
Term Loans						
Domestic currency	19,903	50,000	66,000	86,000	112,000	146,000
Foreign currency						
ADB and IBRD	1,029	13,544	17,488	17,488	17,488	17,488
KFX Fund	-	100	100	200	400	700
Working capital loans	180,269	200,000	264,000	344,000	448,000	584,000
<u>General Populace Loans</u>	200,325	260,000	330,000	430,000	560,000	730,000
<u>Total Approvals</u>	<u>401,526</u>	<u>523,644</u>	<u>677,588</u>	<u>877,688</u>	<u>1,137,888</u>	<u>1,478,188</u>
<u>Commitments</u>						
<u>Business Loans /b</u>						
Term Loans						
Domestic currency	19,903	50,000	66,000	86,000	112,000	146,000
Foreign currency						
ADB and IBRD	584	9,034	14,572	17,487	17,487	17,487
KFX Fund	-	100	100	200	400	700
Working capital loans	180,269	200,000	264,000	344,000	448,000	584,000
<u>General Populace Loans</u>	200,325	260,000	330,000	430,000	560,000	730,000
<u>Total Commitments</u>	<u>401,081</u>	<u>519,134</u>	<u>674,672</u>	<u>877,687</u>	<u>1,137,887</u>	<u>1,478,187</u>
<u>Disbursements</u>						
<u>Business Loans /b</u>						
Term Loans						
Domestic currency	19,903	50,000	66,000	86,000	112,000	146,000
Foreign currency						
ADB and IBRD	-	4,663	11,658	17,487	17,487	17,487
KFX Fund	-	100	100	200	400	700
Working capital loans	180,269	200,000	264,000	344,000	448,000	584,000
<u>General Populace Loans</u>	200,325	260,000	330,000	430,000	560,000	730,000
<u>Total Disbursements</u>	<u>400,497</u>	<u>514,763</u>	<u>671,758</u>	<u>877,687</u>	<u>1,157,887</u>	<u>1,478,187</u>

/a Not including call loan operations which could generate transactions ranging from W 1,740 billion to W 2,547 billion a year, during 1979-83 and temporary investments in securities ranging from W 396 billion to W 559 billion a year during the same projected period. Nor does this table include SMI Promotion Fund loan operations in which CNB is expected to participate beginning 1980.

/b Including manufacturing, mining, transportation, construction and services.

KOREA
THE CITIZENS NATIONAL BANK

Forecast of Resource Position and Requirements, 1980-84

	1980	1981	1982	1983	1984
I. Domestic Currency (Won million) /a					
A. Long-Term Resources					
Uncommitted resources	(149,350)	(214,998)	(289,736)	(364,907)	(468,458)
Net income	5,950	8,512	11,924	15,336	19,598
Noncash charges	16,065	17,930	24,084	32,166	45,192
Government/BOK/KDB and SMIPC loans	1,000	2,000	3,000	4,000	5,000
Net collections on long-term loans	273,920	361,257	471,443	615,028	802,584
Increase in long-term deposits (net of reserve requirement)	66,864	79,864	126,888	161,444	204,305
paid-in share capital	-	10,000	10,000	10,000	10,000
Total Long-Term Resources	214,449	264,565	356,941	471,343	615,635
Less:					
Addition to fixed assets	3,828	4,707	6,075	8,030	9,266
Increase in other long-term assets	2,339	1,794	1,973	2,171	2,387
Net Long-Term Resources for Commitment	208,282	258,064	348,893	461,142	603,982
New Loan Commitments					
Equipment loans	50,000	66,000	86,000	112,000	146,000
Long-term working capital loans	158,000	208,560	271,760	353,920	461,360
Long-term general populace loans	215,280	273,240	356,040	463,680	604,440
Total Commitments	423,280	547,800	713,800	929,600	1,211,800
Year-End Long-Term Resource Position	(214,998)	(289,736)	(364,907)	(468,458)	(603,818)
B. Short-Term Resources					
Uncommitted resources	410,270	507,336	658,505	830,018	1,008,426
Increase in short-term deposits (net of reserve requirement)	147,706	199,388	226,156	282,836	353,545
Collection of short-term loans	56,080	73,981	96,557	125,972	164,416
Total Short-Term Resources	614,056	780,705	981,218	1,238,826	1,526,387
Less:					
Investment in securities	20,000	10,000	5,000	40,000	10,000
Net Short-Term Resources for Commitment	594,059	770,705	976,218	1,198,826	1,516,387
New Loan Commitments					
Short-term working capital loans	42,000	55,440	72,240	94,080	122,640
Short-term general populace loans	44,720	56,760	73,960	96,320	125,560
Total Commitments	86,720	112,200	146,200	190,400	248,200
Year-End Short-Term Resource Position	507,336	658,505	830,018	1,008,426	1,268,187
C. Total Domestic Resources					
Year-end long-term resources	(214,998)	(289,736)	(364,907)	(468,458)	(603,982)
Year-end short-term resources	507,336	658,505	830,018	1,008,426	1,268,187
Year-end Total Domestic Currency Resource Position	292,338	368,769	465,111	539,968	664,205
II. Foreign Currency (US\$ thousand)					
Uncommitted resources	8,998	23,500	28,500	28,500	28,500
Borrowings from:					
ADB	-	30,000	-	30,000	-
IBRD	30,000	-	30,000	-	30,000
KFX Fund	172	172	343	686	1,201
Total Foreign Currency Resources	39,170	53,672	58,843	59,186	59,701
New loan commitments	15,670	25,172	30,343	30,686	31,201
Year-End Foreign Currency Resource Position	23,500	28,500	28,500	28,500	28,500

/a This table does not include SMI Promotion Fund resources and loan operations in which CNB is expected to participate beginning 1980.

KOREATHE CITIZENS NATIONAL BANKProjected Income Statements, 1979-84
(Won million)

	1979	1980	1981	1982	1983	1984
<u>INCOME</u>						
Interest on business loans	48,170	70,588	99,583	137,451	176,928	229,111
Interest on general populace loans	36,795	57,046	87,022	124,271	163,310	213,175
Interest on foreign currency loans	-	149	1,028	2,461	4,293	6,063
Interest on deposits with domestic banks	22,758	30,015	39,372	41,172	46,572	52,272
Interest on securities	24,736	29,374	36,694	41,622	47,022	53,022
Interest on call loans	8,771	5,000	6,250	7,500	13,750	17,500
<u>Total Interest Income</u>	<u>141,230</u>	<u>192,172</u>	<u>269,949</u>	<u>354,477</u>	<u>451,875</u>	<u>571,143</u>
Dividends on investments	7	1,830	2,079	2,256	2,256	2,256
Fees and commissions	1,391	1,692	1,945	2,236	2,572	2,741
Other income	4,643	6,014	6,558	7,460	8,610	8,903
<u>Gross Income</u>	<u>147,271</u>	<u>201,708</u>	<u>280,531</u>	<u>366,429</u>	<u>465,313</u>	<u>585,043</u>
<u>EXPENSES</u>						
Interest on mutual installment receipts	17,773	23,090	31,654	50,783	67,708	84,268
Interest on deposits	77,363	109,785	159,449	199,778	249,173	311,186
Interest on borrowings from BOK/Govt/SMIPC	155	128	421	904	1,586	2,490
Interest on foreign borrowings	-	111	803	1,944	3,391	4,757
Interest on debentures issued	184	676	1,013	1,175	1,404	1,715
<u>Total Interest Expenses</u>	<u>95,475</u>	<u>133,790</u>	<u>193,340</u>	<u>254,584</u>	<u>323,262</u>	<u>404,416</u>
Contribution to Credit Guarantee Fund	1,307	1,082	1,368	1,750	2,253	2,917
General administrative expenses	42,154	57,570	72,867	92,259	116,853	148,054
Other expenses	4,321	550	660	792	950	1,390
<u>Total Expenses</u>	<u>143,257</u>	<u>192,992</u>	<u>268,235</u>	<u>349,385</u>	<u>443,318</u>	<u>556,777</u>
<u>Income Before Provisions and Tax</u>	<u>4,014</u>	<u>8,716</u>	<u>12,296</u>	<u>17,044</u>	<u>21,995</u>	<u>28,266</u>
Provisions for doubtful loans	1,516	1,716	2,282	3,016	3,953	5,210
<u>Income Before Tax</u>	<u>2,498</u>	<u>7,000</u>	<u>10,014</u>	<u>14,028</u>	<u>18,042</u>	<u>23,056</u>
Tax	375	1,050	1,502	2,104	2,706	3,458
<u>Net Income</u>	<u>2,123</u>	<u>5,950</u>	<u>8,512</u>	<u>11,924</u>	<u>15,336</u>	<u>19,598</u>

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THE CITIZENS NATIONAL BANK

Projected Balance Sheets (1979-84)
(Won million)

As of December 31	1979	1980	1981	1982	1983	1984
<u>ASSETS</u>						
<u>Current Assets</u>						
Cash and checks	90,076	122,628	170,342	238,514	279,886	365,813
Due from Bank of Korea	185,053	197,630	252,100	317,550	378,150	472,650
Deposits with other domestic banks	97,153	111,351	118,351	121,851	149,851	156,851
Foreign currency deposits	4	100	200	300	400	500
Short-term loans:						
for business	53,905	67,345	85,825	110,208	142,128	184,632
for general populace	42,377	59,576	79,316	104,576	137,084	178,364
<u>Total short-term loans</u>	<u>96,282</u>	<u>126,921</u>	<u>165,141</u>	<u>214,784</u>	<u>279,212</u>	<u>362,996</u>
Securities maturing within a year	88,379	100,526	106,426	109,326	132,926	138,826
Call loans	-	-	-	-	-	-
Other current assets	6,005	7,206	8,647	10,377	12,452	14,942
<u>Total current assets</u>	<u>562,952</u>	<u>666,362</u>	<u>821,207</u>	<u>1,012,702</u>	<u>1,232,877</u>	<u>1,512,578</u>
<u>Medium/Long-Term Assets</u>						
Medium-term deposits with domestic banks	41,898	47,700	50,700	52,200	64,200	67,200
Term loans in local currency						
for business	266,958	333,518	425,038	545,792	703,872	914,368
for general populace	203,998	286,799	381,821	503,424	659,916	858,636
Term loans in foreign currency						
ADB	-	2,915	7,578	14,418	24,583	30,761
IBRD	-	1,748	8,743	19,235	25,765	35,275
KFX funds	-	100	200	400	800	1,500
<u>Total term loans</u>	<u>470,956</u>	<u>625,080</u>	<u>823,380</u>	<u>1,083,269</u>	<u>1,414,936</u>	<u>1,840,540</u>
Less: provisions for doubtful loans	2,417	4,052	6,889	9,798	12,694	17,552
<u>Net Term Loan Portfolio</u>	<u>468,539</u>	<u>621,028</u>	<u>816,491</u>	<u>1,073,471</u>	<u>1,402,242</u>	<u>1,822,988</u>
Securities	61,947	69,800	73,900	76,000	92,400	96,500
Other medium/long-term assets	15,598	17,937	19,731	21,704	23,875	26,262
<u>Fixed Assets</u>						
Premises and equipment (net)	26,361	30,189	34,896	40,971	49,001	58,267
<u>Deferred Accounts</u>	8	-	-	-	-	-
<u>Total Assets</u>	<u>1,177,303</u>	<u>1,453,016</u>	<u>1,816,925</u>	<u>2,277,048</u>	<u>2,864,595</u>	<u>3,583,795</u>

As of December 31	1979	1980	1981	1982	1983	1984
<u>LIABILITIES AND EQUITY</u>						
<u>Current Liabilities</u>						
Demand deposits	209,790	259,790	322,800	403,400	504,200	630,200
Time and savings deposits	435,958	556,832	723,984	904,755	1,130,832	1,413,428
Property formation savings deposits	2,878	3,009	3,228	4,034	5,042	6,302
Subtotal	<u>648,626</u>	<u>819,631</u>	<u>1,050,012</u>	<u>1,312,189</u>	<u>1,640,074</u>	<u>2,049,930</u>
Debentures issued	1,818	3,430	3,920	4,606	5,586	6,860
Other current liabilities	63,986	76,783	87,139	100,568	132,981	159,881
<u>Total Current Liabilities</u>	<u>714,430</u>	<u>899,844</u>	<u>1,141,071</u>	<u>1,417,363</u>	<u>1,778,641</u>	<u>2,216,671</u>
<u>Medium/Long-Term Liabilities</u>						
Mutual installment receipts	197,299	241,299	298,590	373,145	466,385	582,935
Time and savings deposits	64,344	82,470	97,226	114,000	137,483	169,337
Property formation savings deposits	140,548	147,417	158,172	197,666	247,058	308,798
Subtotal	<u>402,191</u>	<u>471,186</u>	<u>553,988</u>	<u>684,811</u>	<u>850,926</u>	<u>1,061,070</u>
Borrowings from:						
BOK	279	100	200	400	800	1,500
KDB	4	-	-	-	-	-
SMIPC	-	1,000	3,000	6,000	10,000	15,000
Government	423	373	373	173	-	-
ADB	-	2,915	7,578	14,418	24,583	30,761
IBRD	-	1,748	8,743	19,235	25,765	35,275
Debentures issued	35	70	80	94	114	140
<u>Total Medium/Long-Term Liabilities</u>	<u>402,932</u>	<u>477,392</u>	<u>573,962</u>	<u>725,131</u>	<u>912,188</u>	<u>1,143,746</u>
Provision for retirement grants	21,681	32,381	42,381	56,381	74,381	99,381
<u>Equity</u>						
Paid-in capital	30,000	30,000	40,000	50,000	60,000	70,000
Capital surplus	71	71	71	71	71	71
Legal reserves	1,922	2,547	4,297	6,547	9,547	13,297
Other reserves	4,124	4,831	6,631	9,631	14,431	21,031
Retained earnings	2,143	5,950	8,512	11,924	15,336	19,598
<u>Total Equity</u>	<u>38,260</u>	<u>43,399</u>	<u>59,511</u>	<u>78,173</u>	<u>99,385</u>	<u>123,997</u>
<u>Total Liabilities and Equity</u>	<u>1,177,303</u>	<u>1,453,016</u>	<u>1,816,925</u>	<u>2,277,048</u>	<u>2,864,595</u>	<u>3,583,795</u>

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THE CITIZENS NATIONAL BANK

Projected Indicators of Financial Position and Performance, 1979-84
(Won billion)

	1979	1980	1981	1982	1983	1984
I. <u>Total Assets</u>	1,177.3	1,453.0	1,816.9	2,277.0	2,864.6	3,583.8
Of which:						
Short-term loans	96.3	126.9	165.1	214.8	279.2	363.0
Medium/long-term loans	471.0	625.1	823.4	1,083.3	1,414.9	1,840.5
Deposits with other banks	139.0	159.0	169.0	174.0	214.0	224.0
<u>Deposits and Long-Term Debt</u>						
Deposits (less than 1 year)	648.6	819.6	1,050.0	1,312.2	1,640.1	2,049.9
Deposits (more than 1 year)	402.2	471.2	554.0	684.8	850.9	1,161.1
Long-term debt:						
BOK/Government/SMIPC	0.7	1.5	3.6	6.6	10.8	16.5
ADB/IBRD	-	4.7	16.3	33.6	50.3	66.0
<u>Equity</u>	38.3	43.4	59.5	78.2	99.4	124.0
<u>Debt-Equity Relationship</u>						
Total debt/equity ratio	29.2:1	33.6:1	30.5:1	28.9:1	28.4:1	28.4:1
Long-term debt/equity ratio <u>/a</u>	8.0:1	8.8:1	7.7:1	7.5:1	7.4:1	7.5:1
Long-term debt/equity ratio <u>/b</u> (adjusted)	3.7:1	4.1:1	3.5:1	3.4:1	3.4:1	3.5:1
<u>Current Ratio</u>						
Current ratio (adjusted) <u>/c</u>	1.13:1	1.12:1	1.11:1	1.11:1	1.11:1	1.11:1
II. Gross income as % of average						
total assets	14.4	15.3	17.2	17.9	18.1	18.1
Financial expenses as % of						
average total assets	9.3	10.2	11.8	12.4	12.6	12.5
Gross spread (gross income -						
financial expenses)	5.1	5.1	5.4	5.5	5.5	5.6
Income before provisions and tax						
as % of average total assets	0.4	0.7	0.8	0.8	0.9	0.9
Income after provisions and tax						
as % of average total assets	0.2	0.4	0.5	0.6	0.6	0.6
Income after provisions and tax						
as % of average equity	8.7	15.1	17.5	18.3	18.2	18.4
Reserves and provisions as % of						
year-end outstanding loan						
portfolio	2.1	2.4	2.8	3.1	3.3	3.6
General administrative expenses as						
% of average total assets	4.1	4.4	4.5	4.5	4.5	4.6
Book value as % of par value	125	137	141	148	158	169
Cost of deposits as % of average						
deposits outstanding	8.4	9.4	11.0	11.1	11.1	11.1
Cost of term debt as % of average						
term debt outstanding	12.5	5.9	9.2	9.3	9.9	10.0
Cost of foreign currency debt as						
% of average foreign currency						
debt outstanding	-	4.3	7.7	7.6	8.1	8.2
Income from business loans as %						
of average business loans						
outstanding	23.4	19.6	21.8	23.6	23.6	23.5
Income from populace loans as %						
of average populace loans						
outstanding	21.7	19.2	21.5	23.3	23.2	23.2
Income from foreign currency loans						
as % of average foreign currency						
loans outstanding	-	3.6	9.1	9.9	10.1	10.3

/a Long-term debt - current maturities to total equity.

/b Long-term debt + long-term guarantees - current maturities - reserve requirements by BOK - remunerated mutual installment savings to total equity less dividends for current year.

/c Current assets + current maturities to current liabilities + current maturities.

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THE CITIZENS NATIONAL BANK

Projected Cash Flow Statements, 1980-84
(Won million)

Year ending December 31,	1979 (actual)	1980	1981	1982	1983	1984
SOURCES						
Operations:						
Net income	2,123	5,950	8,512	11,924	15,336	19,598
Noncash charges (depreciation & provisions) - net	15,651	16,065	17,930	24,084	32,166	45,192
Subtotal	<u>17,774</u>	<u>22,015</u>	<u>26,442</u>	<u>36,008</u>	<u>47,502</u>	<u>64,790</u>
Increase in deposits:						
Mutual installment receipts	41,528	44,000	57,291	74,555	93,240	116,550
Demand deposits	48,617	50,000	63,010	80,600	100,800	126,000
Savings deposits	144,190	139,000	181,908	197,545	249,560	314,450
Property formation savings deposits	20,426	7,000	10,974	40,300	50,400	63,000
Subtotal	<u>254,761</u>	<u>240,000</u>	<u>313,183</u>	<u>393,000</u>	<u>494,000</u>	<u>620,000</u>
Borrowings:						
BOK/KDB	279	100	100	200	400	700
SMIPC	-	1,000	2,000	3,000	4,000	5,000
ADB	-	2,915	4,663	6,995	10,492	6,995
IBRD	-	1,748	6,995	10,492	6,995	10,492
Others	-	-	-	-	-	-
Debentures issued	2,148	3,465	4,400	5,170	6,270	7,700
Subtotal	<u>2,427</u>	<u>9,228</u>	<u>18,158</u>	<u>25,857</u>	<u>28,157</u>	<u>30,887</u>
Loan collections:						
Business loans	117,023	170,000	220,000	284,863	370,000	477,000
General populace loans	150,211	160,000	215,238	283,137	371,000	490,000
Call loans	3,762,300	1,620,000	2,025,000	2,430,000	4,455,000	5,670,000
ADB subloans	-	-	-	155	327	817
IBRD subloans	-	-	-	-	465	982
Subtotal	<u>4,029,534</u>	<u>3,048,036</u>	<u>4,107,292</u>	<u>5,468,736</u>	<u>8,902,663</u>	<u>12,197,606</u>
Increase in other liabilities	700,342	1,098,036	1,647,054	2,470,581	3,705,871	5,558,807
Increase in paid-in capital	11,200	-	10,000	10,000	10,000	10,000
Sale of securities	95,094	195,000	221,000	234,000	241,000	293,000
Sale of fixed assets	102	150	200	250	300	400
Decrease in other assets	11,285	15,338	17,851	20,148	22,777	25,792
Total Sources	<u>5,134,689</u>	<u>3,529,767</u>	<u>4,714,126</u>	<u>6,187,999</u>	<u>9,746,399</u>	<u>13,242,475</u>
USES						
Disbursement of loans:						
Business loans	200,172	250,000	330,000	430,000	560,000	730,000
General populace loans	200,325	260,000	330,000	430,000	560,000	730,000
ADB subloans	-	2,915	4,663	6,995	10,492	6,995
IBRD subloans	-	1,748	6,995	10,492	6,995	10,492
KFX Fund loans	-	100	100	200	400	700
Call loans	3,672,300	1,620,000	2,025,000	2,430,000	4,455,000	5,670,000
Subtotal	<u>4,072,797</u>	<u>2,134,763</u>	<u>2,696,758</u>	<u>3,307,687</u>	<u>5,592,887</u>	<u>7,148,187</u>
Repayment of borrowings:						
BOK/KDB/SMIPC	1,523	283	-	-	-	-
Government	577	50	-	200	173	-
ADB	-	-	-	155	327	817
IBRD	-	-	-	-	465	982
Others	12,170	-	-	-	-	-
Repayment of debentures issued	534	1,818	3,900	4,470	5,270	6,400
Subtotal	<u>2,634</u>	<u>2,151</u>	<u>3,900</u>	<u>4,825</u>	<u>6,237</u>	<u>8,199</u>
Increase in deposits with domestic banks	141,472	32,673	64,570	70,550	100,700	104,600
Investment in securities	172,414	215,000	231,000	239,000	281,000	303,000
New premises & equipment	1,708	5,000	6,000	7,500	9,600	11,000
Increase in other assets	17,105	18,878	21,086	23,851	27,023	30,669
Payment of dividends	400	811	3,200	4,000	4,800	5,600
Payment of retirement grants	1,228	2,700	4,000	6,000	10,000	14,000
Decrease in other liabilities	686,690	1,085,239	1,636,698	2,457,152	3,673,458	5,531,907
Total Uses	<u>5,108,618</u>	<u>3,497,215</u>	<u>4,667,212</u>	<u>6,120,565</u>	<u>9,705,703</u>	<u>13,157,162</u>

KOREA

THE CITIZENS NATIONAL BANK

Underlying Assumptions for Operational and Financial Projections

I. Operational Projections

Loan Operations

1. In the case of local currency loans, there will be no time lag between approvals, commitment and disbursements.
2. In the case of foreign currency loans around 60% of foreign currency loan approvals are expected to be committed in the current year and 40% in the following year. Around 45% of the commitments are expected to be disbursed in the current year and 55% in the following year. The time lag for foreign currency loans financed with the Korean Foreign Exchange Fund is negligible.
3. Total local currency loan approvals are estimated to reach W 400 billion in 1979 and expected to increase at a rate of 30% thereafter. (The 1979 forecast has been approved by the Ministry of Finance.) Business loans' share in the aggregate commitments will increase by 2% p.a., while general populace loans will decline. Twenty percent of business loans will be for equipment purchases with 80% for working capital purposes.
4. Foreign currency loan approvals are estimated to amount to US\$5 million in 1979, US\$20 million in 1980 and US\$30 million each in 1981-83.

Projected Rates of Increase (Decrease) in Deposits

5. Based on the actual record of the past five years, rates of increase (decrease) in deposits applied for projections are as follows:

Type of deposits	1979 -----	Average 1980-83 (%) -----
Mutual installment receipts	19	19.3
Demand deposits	(9)	19.3
Time & savings deposits	20	19.7
Property formation deposits	(54)	18.0

Investment of Surplus Funds

6. Mobilized funds will be utilized to extend loans after reserves have been deposited with BOK. Any balance will be used for investments in marketable securities and deposited with other banks, at a ratio of 50:50 for such items.

7. The estimated amounts of investments in marketable securities are arrived at on the basis of the average turnover rate (purchase amount for a year as a percentage of outstanding balance at year-end) during the past five years.

8. Since call loans are short term, the year-end balance of such loans is assumed to be zero. the call-loan operations will increase by 10% each year.

II. Financial Projections

Interest Rates

9. Interest income and expenses for local currency operations are calculated by applying relevant interest rates to average balances of loans, borrowings and deposits. A 2% spread on ADB and IRRD loans is included in the projections.

General Administrative Expenses

10. General administrative expenses are assumed to increase at a rate of 27.5% p.a.

Contribution to Credit Guarantee Fund

11. Annual contribution to Credit Guarantee Fund is computed at 0.5% of the average business loans outstanding.

Provision for Doubtful Loans

12. With regard to provisions for doubtful loans, 0.5% of average balance of general populace loans is accumulated to the account of special provisions for doubtful loans, and 0.25% of average balance of foreign currency loans and 0.21% of average balance of business loans are allocated to the account of ordinary provisions for doubtful loans.

Provision for Retirement Grants

13. In addition to regular accumulation, special contribution would be made up to 1980 to cover up the deficit of W 4,204 million.

Dividend Payment

14. Eight percent of paid-in capital.

Share Capital Increase

15. Paid-in capital is increased by W 25 billion in 1979 through cash payment of W 11.2 billion and revaluation of assets amounting to W 13.8 billion.

AEP Projects Department
December 15, 1979

KOREA

THE CITIZENS NATIONAL BANK

Estimated Commitments and Disbursements of Proposed Loan /a
(US\$ million)

	<u>Commitments</u>		<u>Disbursements</u>	
	<u>Amount</u>	<u>% /b</u>	<u>Amount</u>	<u>% /b</u>
<u>FY81</u>				
July-September	4.50	15.0	-	-
October-December	4.50	30.0	3.00	10.0
January-March	4.50	45.0	3.00	20.0
April-June	3.00	55.0	3.00	30.0
Subtotal	<u>16.50</u>	<u>55.0</u>	<u>9.00</u>	<u>30.0</u>
<u>FY82</u>				
July-September	3.00	65.0	3.00	40.0
October-December	3.00	75.0	3.00	50.0
January-March	4.50	90.0	3.75	62.5
April-June	3.00	100.0	3.75	75.0
Subtotal	<u>13.50</u>	<u>100.0</u>	<u>13.50</u>	<u>75.0</u>
<u>FY83</u>				
July-September	-	-	3.75	87.5
October-December	-	-	3.75	100.0
Subtotal	-	-	<u>7.50</u>	<u>100.0</u>
<u>Total</u>	<u>30.00</u>	<u>100.0</u>	<u>30.00</u>	<u>100.0</u>

/a Assuming that the loan would become effective in June 1980.

/b Percentages are cumulative.

AEP Projects Department
February 29, 1980

